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MORTGAGE DISCRIMINATION

HEARING

BEFORE THE

SUBCOMMITTEE ON
CONSUMER AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

ON

THE REPORTS FROM THRIFT REGULATORY AGENCIES AND THE DEPARTMENT OF HUD ON THE EVIL OF RACIAL DISCRIMINATION IN HOME MORTGAGE LENDING AND THE INADEQUATE REGULATORY RESPONSE TO THE SITUATION

MAY 16, 1990

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MORTGAGE DISCRIMINATION

WEDNESDAY, MAY 16, 1990

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:30 a.m., in room SD-538, Dirksen Senate Office Building, Senator Dixon (chairman of the subcommittee) presiding.

Present: Senators Dixon, Riegle, D'Amato, and Bond.

OPENING STATEMENT OF SENATOR DIXON

Senator DIXON. Ladies and gentlemen, the Senate Banking Subcommittee on Consumer and Regulatory Affairs' hearing on discrimination in home mortgage lending will come to order, please.

And may I observe at the outset that I am pleased and honored to note the presence of the distinguished chairman of the Banking Committee this morning, the Senator from Michigan, Senator Riegle.

Ladies and gentlemen, today the subcommittee continues its efforts to remedy the evil of racial discrimination in home mortgage lending. Just over 6 months ago, the various bank and thrift regulatory agencies and the Department of Housing and Urban Development came before this subcommittee to report on statistical evidence of discrimination and suggested remedies. As those of you who attended that hearing know, I was greatly troubled by the statistics which showed that blacks in minority neighborhoods got fewer loans and got rejected for loans more often than whites in white neighborhoods, even when incomes were comparable.

I was equally troubled by the inadequate regulatory response to this situation. I announced at that hearing that we would all gather here again this spring for progress reports and new statistics from the regulatory agencies and HUD.

Our purpose today is to review those reports to see whether there, in fact, has been any progress in this matter. I have reviewed the written testimony and must comment that the news is decidedly mixed:

On the one hand, the agencies appear to have spent some serious time and effort on improving the training of consumer examiners. I commend these efforts to improve Community Reinvestment Act examination techniques and to make them more uniform. That concern was highlighted in a hearing this subcommittee held last

July; although, I must admit, the agencies did little to improve until the public disclosure provisions of FIRREA were passed.

In addition, all of the agencies except for the Comptroller of the Currency have some new initiatives to announce. These efforts are commendable.

Yet, the Office of Thrift Supervision reports that the gap between whites and blacks in home mortgage lending, unbelievably, has widened. Even so, over the past 3 years throughout the entire United States of America the regulatory agencies, while conducting thousands of examinations, found only six or seven substantive violations of fair lending laws prohibiting mortgage discrimination. That's in 3 years. And no agency has yet seen fit to refer any cases whatsoever to the Justice Department for further investigation or prosecution.

The financial regulatory agencies may see, hear and speak no evil, but I believe that the evidence demonstrates that discrimination in mortgage lending does still exist in this country. I believe that this evil hurts people: working families who have earned their fair share of the American dream. And I further believe that this evil is stoppable. We are here today to find new ways to ensure the laws are enforced.

Now, I thank my distinguished friend from Michigan, the chairman of the committee, for being here; does he have any opening statement?

Senator RIEGLE. Thank you, Senator Dixon.

Senator DIXON. The Senator from Michigan.

OPENING STATEMENT OF SENATOR RIEGLE

Senator RIEGLE. I appreciate having the chance to make a few observations.

First of all, let me commend you for your steady and important work in this area and the work of your subcommittee. I think this is clearly a problem that we need to solve, and I mean make sure that we have the ways and means to get it solved. We've seen examples all across the country of patterns of discrimination occurring. It's obviously uneven from area to area. We've had some difficulties in our own State, although efforts have been made to remedy that by institutions in our State acting affirmatively to overcome some of the patterns that have developed.

But I think we need to know whether the regulators who are charged with enforcement of lending antidiscrimination laws are actively monitoring potential violations and really making sure that offenses are being stopped. So I'm going to be particularly interested in hearing from all of our witnesses today in that respect.

I also hope that they will share with us what additional tools may be needed to deal with lenders who persist in discriminatory practices. I think also we need to know when the information required under the Community Reinvestment Act and the Home Mortgage Disclosure Act will be readily available for review by the public as prescribed by FIRREA. And I think then finally we need to know what additional legislative or regulatory actions are necessary and should be taken on to end discriminatory lending practices.

So this is a very important issue that we're dealing with today and I'm very much supportive of your work and that of the subcommittee, Senator Dixon.

Senator **DIXON**. I thank you, Senator Riegle.

The first panel of regulators consists of John P. LaWare, Member, Board of Governors of the Federal Reserve System; Gordon Mansfield, Assistant Secretary for Fair Housing and Equal Opportunity, Department of Housing and Urban Development; Robert J. Herrmann, Senior Deputy Comptroller for Bank Supervision Policy, Office of the Comptroller of the Currency; John F. Bovenzi, Deputy to the Chairman, Federal Deposit Insurance Corporation; Jerauld C. Kluckman, Director, Compliance Programs, Office of Thrift Supervision. We are delighted to have you all here. I think, if it's all right with you, Mr. LaWare, we'll start in your corner.

STATEMENT OF JOHN P. LaWARE, MEMBER, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

Mr. **LAWARE**. Thank you, Mr. Chairman, Senator Reigle.

Thank you very much for this opportunity to speak to the subcommittee in a follow-up on our testimony on mortgage lending discrimination last October. I am pleased to report to you on the progress made on the initiatives envisioned at that time, as well as other activities developed more recently. We have had our hands full in the past few months working on our own and jointly with our sister agencies on several projects that we believe show considerable promise.

On an interagency level, our primary focus over the past several months has been on two major fronts: Uniformly implementing the FIRREA provisions for public disclosure of CRA performance evaluations, and developing the expanded coverage of the changes to the Home Mortgage Disclosure Act.

The new provisions of CRA and HMDA represent a considerable challenge for us. Their combined impact in putting more information in the public domain about the mortgage lending activities of institutions will foster a more open and productive dialog between those institutions and the people that they serve.

We also feel that the impact will bolster the institutions' own awareness of their image and record as lenders and will further our efforts to promote compliance with both the letter and the spirit of the antidiscrimination laws.

CRA CHANGES MANDATED BY FIRREA

Putting in place the CRA changes mandated by FIRREA, including developing uniform examination guidelines with public input, amending our regulations and designing and conducting the interagency examiner training sessions for several hundred examiners has consumed a great deal of the agencies staff time.

At the same time, work proceeded on equally significant changes to the Home Mortgage Disclosure Act, which has been expanded to include the race, sex, and income of borrowers and loan applicants. These provisions should better equip us to determine whether mortgage credit standards are being fairly applied and to judge a given lender's efforts in the context of a more complete picture of the entire mortgage market.

Because the Federal Reserve Board has rule-writing responsibility for the regulation implementing HMDA, the Board worked closely with the Exam Council agencies and HUD to draft the regulatory amendments and to develop a new loan register format. Final amendments to HMDA were issued by the Board effective on January 1.

IMPLEMENTING THE NEW HMDA PROVISIONS

Now our job with respect to implementing the new HMDA provisions has yet another phase. Since HMDA's enactment in 1975, the Board has acted as the agent for the exam council to compile and aggregate the data and to produce tables which represent lending patterns by factors such as racial composition and income characteristics of the neighborhood, as well as the age of the housing stock.

Anticipating a significant increase in the volume of data to be reported next year for 1990, we are working to enhance our data processing capabilities, to encourage electronic submission of data from lenders through our Federal Reserve Banks in order to expedite its ultimate availability to the public and to develop new disclosure formats in order to give a concise presentation of lending patterns using the new data.

We have moved ahead on another interagency initiative as well. Through the Exam Council, we are reviewing the information that has been gathered on mortgage review boards to explore whether and how we should proceed in encouraging their formation on a wider scale. The agencies have also revised an Exam Council publication entitled "A Guide to HMDA Reporting: Getting it Right!" in order to facilitate accurate reporting under the law's new requirements.

And we have agreed to prepare a brochure for lenders discussing how to avoid practices that may result in unfair lending patterns or the appearance of them. We are also taking steps to share among the agencies information gained by our examiners from contacts with members of the community and to make better use of the HMDA data.

Now let me describe some of the initiatives that the Federal Reserve System has on its own been utilizing to strengthen our enforcement efforts and to address our fair lending concerns.

We have been participating in a series of HUD seminars dedicated to fair housing and fair lending issues which have been conducted at selected law schools. We have written to nearly 700—and I believe this is unprecedented—we have written to nearly 700 fair housing and civil rights groups seeking their cooperation in referring to us consumers who feel that they may have experienced discrimination.

We have begun drafting a brochure designed for home buyers describing the credit granting process and the antidiscrimination protections available to them under the law. We are developing a computer software scheme to generate an executive summary of a given institution's HMDA data, comparing its lending patterns to that of its entire peer group in the community for use by our examiners and by the senior officers of the institution itself, so that they do not have to go into the detail of the full report but will have a capsule picture for discussion.

We have enlisted the assistance of Reserve Banks in developing a new on-line consumer complaint and inquiry tracking system that is to be implemented early in 1991 which we envision will enhance the Board's ability to monitor and analyze its consumer complaint data and to more easily spot trends that might indicate illegal credit discrimination.

The resources of our Reserve Banks have also been utilized in various other ways to promote sound and creative lending that is responsive to the special needs of low- and moderate-income communities. Specific initiatives are detailed in our written testimony.

Further, we have enlisted the help of the Federal Reserve's Consumer Advisory Council, which has commissioned a committee to look into various aspects of credit discrimination, including mortgage review boards, examination procedures and examiner training, the use of testers, additional studies, and brochures that give guidance to lenders. And we have paid particular attention this year to adding some new members with expertise in the civil rights area, including Professor George Galster of the College of Wooster and Bernard Parker who testified before this committee last year.

Finally, we have taken a close look at our examination and consumer complaint experience over the past 3 years and we will continue to monitor our enforcement and complaint activities to ensure that practices involving possible racial discrimination are addressed and corrective action is taken as needed. The new data and procedures I have mentioned above will help us in this effort.

In closing, on our own and in collaboration with our fellow agencies, we have completed a number of major initiatives. And although we are in the early stages of some others, we believe that they all have considerable promise.

Thank you for inviting me to share with you the progress we have made over the past few months and I will be happy to answer any questions you may have.

[The complete prepared statement of John LaWare follows:]

For release on delivery
9:30 a.m., E.D.T.
May 16, 1990

Statement by

John P. LaWare

Member, Board of Governors of the Federal Reserve System

before the

Subcommittee on Consumer and Regulatory Affairs

of the

Committee on Banking, Housing, and Urban Affairs

United States Senate

May 16, 1990

Summary of Testimony

This testimony is presented as follow-up to the mortgage lending discrimination testimony delivered last October. It describes the progress that has been made on initiatives envisioned at that time, as well as other activities developed more recently. Efforts have been completed or developed in cooperation with the other agencies or individually by Board and Reserve Bank staff.

On an interagency level, efforts have been primarily focused on two areas: implementing the provisions contained in the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) requiring the agencies to prepare and to make public written evaluations of institutions' CRA performance, based on examination findings, along with the ratings assigned using a descriptive, 4-tiered rating system; and fulfilling the changes to the Home Mortgage Disclosure Act (HMDA), which expand the coverage of the Act to include mortgage lenders not affiliated with depository institutions and broaden the scope of data collected to include the race, sex and income of borrowers and loan applicants, as well as the disposition of applications. To implement the new CRA provisions uniformly, the agencies--under the umbrella of the Financial Institutions Examination Council (FFIEC)--are training over 800 of their examiners on how CRA performance should be translated into the public disclosures, and emphasizing consistent application of the new rating scheme and the importance of thorough, insightful and well-supported evaluations.

Other interagency initiatives that have been addressed since the October testimony include reviewing information gathered on mortgage review boards to explore whether, and how, the formation of such boards should be encouraged on a wider scale; and revising the FFIEC publication A Guide to HMDA Reporting: Getting It Right! to facilitate accurate reporting under the law's new requirements. The FFIEC has also approved plans to produce a brochure targeted to mortgage lenders, consented to developing procedures for facilitating the sharing amongst the agencies of community contact information gained during the course of CRA examinations, and accepted an initiative to make better use of HMDA data.

In addition to these interagency initiatives, the Federal Reserve System has, on its own, been utilizing various avenues to strengthen enforcement efforts and to bring constructive approaches to resolve fair lending concerns to the forefront of public attention. Federal Reserve Board staff is in the process of drafting a brochure for homebuyers, has written to several hundred fair housing and civil rights-oriented groups to seek their cooperation in referring complainants to the appropriate regulatory agency, and has been participating in a series of HUD seminars dedicated to fair housing/fair lending issues at law schools. Additionally, developments in Atlanta, Detroit and

Boston are being monitored, and work has begun on developing computer software to generate a concise presentation of a given institution's mortgage and home improvement lending patterns in comparison with the record of lenders as a whole in the community.

The Board, with the assistance of Reserve Bank staff, has begun work on a new on-line consumer complaint and inquiry tracking system to be implemented in early 1991. The resources of the Reserve Banks are being utilized in a number of other ways to promote sound and creative lending that is responsive to the special needs of low and moderate income communities.

The Board has also enlisted the help of the Federal Reserve's Consumer Advisory Council and has sought to draw on the expertise of individuals and groups outside the bounds of the federal financial regulatory framework to gain a fresh perspective on our enforcement activities. Reserve Bank examination and consumer complaint experience over the past three years has been closely studied and will continue to be monitored to ensure that practices involving possible racial discrimination are addressed and that corrective action is taken as needed. This will be aided by the new data and procedures discussed in the testimony.

* * * * * * * * * * * * * * * *

Testimony before

Subcommittee on Consumer and Regulatory Affairs

Senate Committee on Banking, Housing and Urban Affairs

May 16, 1990

Thank you very much for this opportunity to speak to the Subcommittee in follow-up to our testimony on mortgage lending discrimination last October. I am pleased to report to you on the progress made on initiatives envisioned at that time, as well as other activities developed more recently through the Federal Reserve System's ongoing programs to ensure equal access to housing credit and to promote private sector reinvestment in low and moderate income communities.

On an interagency level, our efforts have been focused for the past several months on two major fronts, both of which have important implications for our work in enforcing fair housing and fair lending laws. The first involves changes in the Community Reinvestment Act (CRA), under which the agencies have been charged with encouraging financial institutions to help meet the credit needs of their entire communities, for example, for housing, small business, rural economic development, and with assessing their performance in doing so. Traditionally, those CRA assessments, like all other findings reached by the agencies during the course of examinations, have been kept strictly confidential as part of the supervisory dialogue between us as regulators and the institutions we supervise.

Starting with examinations conducted on or after July 1 of this year, that tradition will be broken in a dramatic way. Provisions contained in the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) require the agencies to prepare and to make public written evaluations of institutions' CRA performance, based on our examination findings, along with the ratings assigned using a descriptive, 4-tiered rating system. This mandate makes clear the need for a concerted effort by all four agencies, under the umbrella of the Federal Financial Institutions Examination Council (FFIEC), to take a uniform approach to assigning ratings, presenting the evaluations in a consistent, readily understandable manner and insuring that the public has access to these evaluations.

That is precisely what we have tried to do, through the efforts of the FFIEC. The FFIEC spearheaded the development of draft guidelines for implementing the CRA changes, which were issued for public comment last December. In light of input received from community organizations, financial institutions, members of the Congress and others, the guidelines were finalized by the FFIEC last month and it is currently putting on an extensive training program and revising the interagency examination procedures for CRA.

At the same time, work proceeded on equally significant changes to the Home Mortgage Disclosure Act (HMDA), which expand the coverage of the Act to include mortgage lenders not affiliated with depository institutions or holding companies -- effectively bringing all types of mortgage lenders in the U.S. under the Act. The scope of data collected has also been expanded to include the race, sex and income of borrowers and loan applicants, as well as the disposition of applications (approval, denial, or withdrawal by the applicant). These provisions should better equip us to determine whether mortgage credit standards are being fairly applied, and to judge a given lender's efforts in the context of a more complete picture of the entire mortgage market. Because the Federal Reserve Board has rulewriting responsibility for the regulation implementing HMDA, Board staff worked closely with staff members from the FFIEC agencies and HUD to draft the regulatory amendments and to develop a new loan register format designed to make the increased reporting requirements less cumbersome for lenders. After receipt of public comment, final amendments to HMDA were issued by the Board last December and became effective on January 1, 1990.

Our job with respect to implementing the new HMDA provisions has yet another phase, however. For the many years since HMDA's enactment in 1975, the Board has acted as the agent for the FFIEC to compile and aggregate the data, and to produce tables which present lending patterns by factors such as the racial composition and income characteristics of the neighborhood as well as the age of housing stock. Anticipating a significant increase in the volume of data to be reported next year for 1990, we are working to enhance our data processing capabilities, to encourage electronic submission of data from lenders through our Federal Reserve Banks to expedite its ultimate availability to the public, and to develop new disclosure formats in order to give a concise presentation of lending patterns using the new data.

These changes to both the CRA and HMDA represent a considerable challenge for us. We are very much aware that the public disclosure provisions make the CRA examination process subject to greater scrutiny than ever before. It will be incumbent on our examiners to discuss each of the assessment factors relating to the State member bank's performance -- including the assessment factor relating to discrimination or other illegal credit practices -- and to show how each factor impacts overall performance. They must fully justify their conclusions and assigned rating, without divulging the institution's financial condition, information about its employees or customers, or anything else the law instructs us to keep confidential. The new HMDA data promise to be valuable in the rating process, but usefulness will largely depend on the examiners' ability to analyze it and to draw appropriate conclusions from it.

A major step toward meeting the challenge is the interagency examiner training program being carried out this month at four locations nationwide. It involves eight sessions for approximately 800 examiners from the bank regulatory agencies. The training gives examiners guidance on how the disclosures should be prepared, how the rating system should be applied, and emphasizes the importance of thorough, insightful and well-supported evaluations.

While the spotlight is sure to fall on the work of our examiners after July 1, to an even greater degree the attention will fall on financial institutions themselves, and how well they are, or are not, helping to meet local credit needs. The new CRA and HMDA provisions come at a time when public concern for affordable housing, the adequacy of financial services within reach of the less affluent, the problems of economic development and growth, and the need to assure fair lending practices, runs high. Their combined impact in putting more information in the public domain will, we hope, foster a more open and productive dialogue about such concerns between financial institutions and the people they serve. We are also hopeful that the impact will bolster institutions' awareness of both their image and record as a fair lender, and will further our efforts to promote compliance with the letter and spirit of the antidiscrimination laws.

Putting in place the changes mandated by FIRREA and the examiner training sessions have consumed a great deal of the agencies' staff time, especially of those having expertise in the fair lending and fair housing arena. Nevertheless, we have moved ahead on other interagency initiatives which I outlined when I last appeared before the Subcommittee.

Through the FFIEC, the agencies have begun to take a close look at the concept of mortgage review boards, which brings together lenders and community representatives to provide an appeals mechanism in cases where applicants feel they have been unfairly denied credit for purchasing a home. As a first step, inquiries were made through the agencies' field offices around the country to determine the extent to which mortgage review boards exist. Follow-up visits were then made to Massachusetts and Michigan (the two states where functioning boards were identified) to learn how they operate, the kinds of support they require and the degree of success each has achieved. The FFIEC is reviewing the information gathered to explore whether, and how, the formation of such boards should be encouraged on a wider scale. Initially a matter of concern is the very small number of appeals which have been brought forward in the experience of both states, and whether other, quite different localities around the country would be receptive to the notion.

In the course of its study, the FFIEC's attention was drawn to a somewhat similar vehicle which may have favorable prospects for replication in other communities. Under the Philadelphia Mortgage Plan, a group of large commercial banks agreed to refrain from rejecting mortgage applicants until the credit committee representing all PMP lenders has an opportunity to review the case and, if possible, place the loan with one of the other participating lenders. The lenders also offer "creative" mortgage products by providing some flexibility in underwriting criteria, such as considering rent receipts, landlord references and utility bill payments to help establish credit histories. In its 15 years of existence, the Plan has secured loans for 13,000 families totalling $180 million, and was expanded to cover the entire Delaware Valley in January of this year. The FFIEC is committed to exploring this approach, as well as others which have worked well in widening access to mortgage credit in lower income and minority neighborhoods.

Another focus of our initiatives is education -- for consumers as well as for lenders -- on their rights and responsibilities under the law. Federal Reserve Board staff is in the process of drafting a brochure designed to better acquaint potential homebuyers with the mortgage origination process, the factors lenders usually consider in determining whether a person is creditworthy, and the statutory protections and agency procedures which provide recourse to those who believe they have been subjected to unlawful discrimination. The FFIEC has also approved plans to produce a brochure targeted to mortgage lenders discussing how to avoid practices that may, even unintentionally, result in unfair lending patterns, or the appearance of them. We anticipate that both brochures will be ready for distribution in the second half of this year.

The emphasis on consumer education stems, at least in part, from our concern about the very small number of complaints we and our sister agencies have received over the years alleging illegal credit discrimination. In an effort to make our work in investigating and responding to such complaints more visible, we have written to several hundred fair housing and civil rights-oriented groups to reacquaint them with our role in enforcing the legal protections afforded loan applicants, and to seek their cooperation in referring complainants to us.

Our testimony last October voiced the belief that much could be gained by the agencies sharing among themselves the information obtained through interviews with community contacts -- including consumer advocacy and housing organizations, local businesspeople, trade associations, realtors, government officials and many others -- during the course of CRA examinations. Their perceptions about the state of the local economy, what types of credit would most help the community grow and prosper, the role played by financial institutions in addressing credit needs, and whether credit is available to minority and low- and moderate-income persons have proved valuable to examiners in making a balanced assessment of CRA performance. I am pleased to say that the FFIEC has approved going forward with procedures for facilitating that flow of information.

We believe we should aim not only to share the information we develop among fellow regulators, but also to communicate effectively with institution management about what we find in analyzing their lending data. This effort takes on particular importance in light of the recently expanded HMDA requirements, and the additional insight regarding lending patterns that the data should provide. With this in mind the FFIEC has approved an initiative to make better use of the HMDA data. Additionally, we are working to develop what might best be termed an "executive summary" of HMDA data -- a succinct presentation of a given institution's mortgage and home improvement lending patterns broken down by demographic factors such as race and income, and compared with the record of lenders as a whole in the community. This summary could be conveyed to institution management during a CRA examination. By providing such a profile, we hope to draw management's attention to market segments the institution may be failing to reach, and to prompt a thorough self-assessment of geographic lending patterns and the reasons for them. Because it is being developed in tandem with the computer applications to accommodate the new HMDA data, the summary probably will not be completed until 1991, although Board and Reserve Bank staff have been testing for several months the use of a very preliminary model. We have also revised the FFIEC publication A Guide to HMDA Reporting: Getting It Right! to facilitate accurate reporting under the law's new requirements.

In addition to these interagency initiatives, the Federal Reserve System has, on its own, been utilizing various avenues to strengthen our enforcement efforts and to bring constructive approaches to resolve fair lending concerns to the forefront of public attention. For example, the Federal Reserve Board has continued to monitor closely developments in Atlanta, Detroit and Boston. This effort has taken several forms. First, the Board has updated the statistical analysis presented in the Atlanta and Detroit newspapers to take account of the availability of more recent HMDA data. The 1987 and 1988 HMDA data continues to show disparities in home mortgage and home improvement lending. As before, predominately white middle-income neighborhoods received more home purchase loans per single family housing unit than did predominately minority middle-income areas, while the opposite pattern holds for home improvement loans. However, as we have indicated in prior testimony while these patterns are suggestive of lending problems in the home purchase area they do not allow one to conclude whether discrimination exists or not.

The Board, with the assistance of Reserve Bank staff, has also begun work on a new on-line consumer complaint and inquiry tracking system to be implemented in early 1991. We envision that the new tracking system will enhance the Board's ability to monitor and analyze its consumer complaint and inquiry data, including data involving allegations of illegal credit discrimination. We expect that the new system's reporting capabilities will enable us to spot more easily trends that might involve such practices.

We are using the resources of our Reserve Bank's in a number of ways. The Federal Reserve Bank of Atlanta has developed a computer model that illustrates how various lending parameters effect the affordability of home loans in connection with the lending consortium established for low- and moderate-income residents of Atlanta. The Federal Reserve Bank of Boston, together with the Boston Federal Home Loan Bank, recently cohosted a symposium of the National Association of Affordable Housing Lenders attended by more than 300 lenders from New England as well as others from throughout the country. Last year the Federal Reserve Bank of San Francisco was instrumental in the creation of the California Community Reinvestment Corporation (CCRC), a lender consortium pooling more than $100 million to provide long-term loans for affordable housing development throughout the state. With the California consortium off to a successful start, Reserve Bank senior management and staff have been invited to Hawaii and Nevada to help bankers and community organizers launch similar programs in those states. Late last year, the Federal Reserve Bank of Chicago convened a seminar with some 250 area bankers to discuss specific CRA-related policies and activities which have worked well in that Federal Reserve District. In Philadelphia, the Federal Reserve Bank is planning to produce a video which will share some of the experiences and lessons learned relating to the CRA. This is but a sample of the activities of Reserve Banks undertaken in the past six months to promote sound and creative lending that is responsive to the special needs of low and moderate income communities. At the Board level, in addition to the initiatives discussed above, Board staff has been participating in a series of HUD seminars dedicated to fair housing/fair lending issues at law schools.

We have also enlisted the help of the Federal Reserve's Consumer Advisory Council. In selecting new members this year, we gave special attention to adding council members who have expertise in the civil rights area. One of the new members, Bernard Parker, testified at your hearing last October. He is executive director of Community Resource Projects, a human services organization based in Detroit that helps economically depressed individuals. Mr. Parker is also Chairman of the Ad Hoc Coalition on Fair Banking Practices in Detroit which was actively involved in a recent financial settlement with banks calling for reinvestment in low-income neighborhoods.

The Board also appointed George C. Galster, Professor of Economics at the College of Wooster. Professor Galster is widely recognized as an expert in discrimination issues. He has been an expert witness and consultant in fair housing disputes and currently is a research consultant for the Metropolitan Milwaukee Fair Housing Council. He also serves on the advisory board for the HUD National Housing Discrimination Survey.

A special committee of the Consumer Advisory Council is looking into various aspects of the issue including mortgage review boards, examination processes and examiner training, the use of testers, additional studies, and brochures that give guidance to lenders. Over the years we have often received helpful input from the Council and we feel fortunate to have this resource to assist us in this difficult area.

We have also sought to draw on the expertise of individuals and groups outside the bounds of the federal financial regulatory framework to gain a fresh perspective on our enforcement activities. Our staff has been in contact with representatives of the National Fair Housing Alliance to arrange for a briefing on their experience with credit discrimination cases. I have personally met with representatives from a civil rights group from Boston that was active in working with the Massachusetts Bankers Association on an ambitious housing and economic development program that is an outgrowth of the Boston Fed's mortgage discrimination study. We have consulted with the Department of Justice about its experiences in civil rights enforcement and its investigation, now in progress, of housing lending practices in Atlanta.

In line with the subcommittee's questions regarding our enforcement program (our detailed responses to the committee's questions accompany our testimony) we have taken a close look at our examination and consumer complaint experience over the past three years. In particular we have completed a detailed analysis of System enforcement activity involving serious violations of the Fair Housing and Equal Credit Opportunity Acts by reviewing our examination and consumer complaint data bases. Additionally, we have asked experienced staff at the Reserve Banks for the types of problems they are seeing involving the Fair Housing and

Equal Credit Opportunity Acts and mortgage lending in particular. As we said at the October hearing, State member banks do not play a major role in the granting of mortgage credit in the United States. Examiners routinely review available mortgage lending data, including lending standards and appraisal practices. While we find violations during examinations and receive a few complaints involving the fair lending statutes, they typically involve marital status issues, such as improperly required spousal signatures. Only in very isolated cases do we find practices that involve racial discrimination in lending. From our discussions with examiners we know that they take their work and the issue of possible racial discrimination very seriously. They have been and will continue evaluating quite closely any questionable lending practices that could "effectively" result in subtle discrimination. We will continue to monitor our enforcement and complaint activities to ensure that practices involving possible racial discrimination are addressed and that corrective action is taken as needed. The new data and procedures I have mentioned above will help us in this effort.

In short, we have had our hands full in the past few months completing a number of major initiatives. And although we are in the early stages of development with others, we believe they have considerable promise, and will be pleased to report to you further on their progress.

Appendix to Testimony

1. In how many instances over the past three years has your agency found substantive violations of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations? Provide some examples of how these substantive violations were resolved.

Over the last three years 163 state member banks have been required to take corrective action for violations of the Equal Credit Opportunity or Fair Housing Acts in accordance with the interagency supervisory enforcement policy. Less than 7% of the banks were cited for violations involving mortgage lending; each of these cases involve marital status discrimination not racial discrimination, where it is easier to establish that a violation has occurred. Although examiners have not been able to establish clear cut violations involving racial discrimination, it is not uncommon for them to raise questions about transactions to help assure that bank customers are being treated fairly.

When a substantive violation of the enforcement policy is found, the institution is required to correct the violation both retrospectively and prospectively. For example, if the violation involves a spousal signature on an obligation where the signature should not have been required under the bank's lending standards, the bank must identify all affected loan files and inform the individuals that the signature will be released unless that spouse wants to remain a signatory on the debt; and if the violation involves loan denial notices that are incorrect the bank must identify all affected individuals and send corrected notices to them. In either case, the bank will be required to discontinue the illegal credit practice and train its employees regarding the provisions of the law.

2. In how many instances over the past three years has your agency referred cases of possible discrimination to the Department of Justice for prosecution? What were the results?

Section 706(g) of the Equal Credit Opportunity Act states that the Board is authorized to refer matters to the Attorney General when we are unable to obtain compliance with requirements of the Act. Section 808(d) of the Fair Housing Act requires the Board to enforce the provisions of the act in an affirmative manner. Our enforcement authority and stated responsibilities under the statutes and Section 8 of the Federal Deposit Insurance Act have been sufficient to require state member banks to comply with the ECOA and FHA; consequently the Board has not referred cases to the Attorney General.

3. Has your agency found violations of the Fair Housing Act or ECOA (Regulation B) based on an "effects test" analysis? Can you provide any specific examples of how you have used this approach

to prohibit lenders from maintaining loan policies which have a discriminatory effect on minorities?

System examination procedures specify that examiners must determine if women or minorities or other protected groups are treated less favorably under the bank's articulated standards for each type of credit that the bank makes available to its community. However, as indicated in our response to Question No. 1, the Board has not found violations of the Equal Credit Opportunity or Fair Housing Acts involving racial discrimination in mortgage lending over the last three years. When violations in mortgage lending are found they typically involve improperly required spousal signatures not racial discrimination.

Examiners occasionally find policies that may have the "effect" of discriminating against a protected class. This finding is rare, however. As an example of such a situation examiners report a case where a comparison of the bank's accepted and rejected loan applications and its minimum lending policy showed a disparate lending pattern that appeared to disfavor women and minorities in the bank's community that were applying for consumer credit (not mortgage credit). The examiners consequently reported that the bank's policy appeared to have the effect of discriminating against women and minorities. As indicated below, occasionally questions have been raised about appraisal policies.

4. How many fair lending written complaints did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation. Provide some examples of how these substantive violations were resolved.

From January 1, 1987 through February 28, 1990, the System received 428 complaints involving the Equal Credit Opportunity Act and the Fair Housing Act. Of these, 262 complaints involved state-chartered banks. The remainder of these complaints were referred to the appropriate regulatory agencies for response.

Only 29 complaints about state member banks involved allegations about mortgage or home improvement lending. The complaints involved a wide range of fact situations and no patterns or trends were apparent. Few of them alleged racial discrimination. In no case did we find a substantive violation of the ECOA or the FHA. Although the financial institutions involved were not found to have discriminated against the complainants, in a few instances the bank granted the applicant credit after further review of the application.

5. How many fair lending telephone calls did your agency receive over the past three years? Can you characterize these inquiries? Are there any patterns among these inquiries? What are complainants told in response?

In the past three years, the System received 26 complaints by telephone involving the ECOA or FHA; however, our data collection system does not break down this figure by the type of credit involved. Therefore, we are unable to determine if any of the 26 telephone complaints involved mortgage lending, although it is possible that some did. When complaints are received by telephone that involve illegal discrimination or complex fact situations, consumers are generally encouraged to submit their complaints in writing to facilitate the Reserve Bank's investigation of the matter. When complainants follow-up their complaints in writing, they are considered for purposes of the tracking system to be written complaints and are handled as described above.

6. Do appraisers, private mortgage insurers, or the secondary market play a role in discrimination? What should Congress do about the problem of under-appraisals of properties in minority areas? Would your agency detect this problem in its normal examination or complaint-response procedures?

We do not know the extent, if any, to which, appraisers, mortgage insurers, and the secondary market play a role in discrimination. Consequently, we do not have any recommendations for Congress in this area. Senior examiners surveyed in connection with this testimony report that they do not see loan denials that they believe are discriminatory involving either the inability to obtain private mortgage insurance for a loan or sell the loan in the secondary market. Examiners report that occasionally suspicious appraisal practices are detected that necessitate an expanded review of the bank's practices, and banks have been advised to change practices that may have a discriminatory effect.

The Board is in the process of developing a rule that will require that appraisals be performed in writing and in accordance with uniform standards as required by FIRREA. Title XI of the act requires the Board and the other regulators to issue regulations to protect federal financial and public policy interests in real estate transactions by requiring the services of an appraiser. Regulations were proposed by the agencies earlier this year that set minimum appraisal standards for "federally related" transactions. Pursuant to Section 1110 of Title XI, the proposed standards require conformity with the Uniform Standards of Professional Appraisal Practice, as adopted by the Appraisal Foundation. These standards state that "an appraiser must avoid stereotyped or biased assumptions relating to race, age, color, religion, gender, or national origin or an assumption that racial, ethnic, or religious homogeneity is necessary to maximize value in a neighborhood. Further, an appraiser must avoid making an assumption or unsupported premise about neighborhood decline, effective age, and remaining life." Our examiners will be alert to any suggestion that these standards are not being followed.

Senator **Dixon**. I thank you for your report, Mr. LaWare.

Mr. **Mansfield**. We're delighted to have you here.

STATEMENT OF GORDON H. MANSFIELD, ASSISTANT SECRETARY FOR FAIR HOUSING AND EQUAL OPPORTUNITY, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, ACCOMPANIED BY RONALD ROSENFELD, DEPUTY ASSISTANT SECRETARY FOR SINGLE FAMILY HOUSING

Mr. **Mansfield**. Thank you, Chairman Dixon, and also Chairman Reigle, for the opportunity to be here this morning to report on the Department of Housing and Urban Development's progress in eliminating discrimination in home mortgage lending since your last hearing in October 1989.

I am accompanied today by Ron Rosenfeld, HUD's Deputy Assistant Secretary for Single Family Housing.

ENFORCEMENT EFFORTS

First, let me describe our enforcement efforts under the Fair Housing Act. Improvements to our data system since last October enable me to provide you with more detail than we did then. From October 1, 1987 to April 24, 1990, we received 342 complaints alleging lending discrimination or redlining.

Prior to March 12, 1989, HUD had no enforcement powers so our efforts were limited to attempting conciliation of these complaints. Subsequent to March 12, 1989, HUD has the power to issue a charge in any complaint which is not conciliated if there is reasonable cause to believe that discrimination has occurred; although most cases are resolved through conciliation or closed administratively before HUD does issue a charge. A charge must be issued before a finding of substantive violation, which can be made only by an administrative law judge or Federal district court.

Of the 342 complaints received from 1987 to 1990, 155 were closed administratively, and we determined not to resolve 136. Fourteen of the complaints were successfully conciliated, two were unsuccessful, and 35 complaints are still pending.

Significant settlements include: $28,000 to complainants who alleged that a full service commercial bank had denied their mortgage application based on their national origin; and a $150,000 loan which had allegedly been denied by a savings and loan association based on race was issued. The complainant could select the interest rate at the time of application or settlement.

Among the cases under investigation are: allegations by a midwestern builder that a local bank discriminated against him by refusing to provide loans in a predominantly minority neighborhood; and another one were allegations that residents of minority neighborhoods in a particular community are steered to FHA loans rather than conventional loans and to mortgage bankers rather than depository institutions, resulting in higher interest rates.

In addition, as data begin to flow into the Department on rejected, as well as accepted, applicants, we expect to identify appropriate lenders for Secretary-initiated investigations under title 8.

I am also pleased to report that the HMDA data for all single family FHA loans by census tract for 1980 to 1989—which HUD is charged with making available—were delivered last week to the Federal Financial Institutions Examination Council. These data should be available for public use by July 15, 1990, and this will fulfill Secretary Kemp's commitment which Assistant Secretary Fitts made to this subcommittee in October.

As we said we would in our testimony last fall, we have worked with the FFIEC to measure, detect and eliminate redlining and other discriminatory practices.

We have been invited to participate formally in the HMDA subcommittee of the FFIEC Consumer Compliance Task Force. HUD has accepted this invitation and agreed to pay its appropriate share of HMDA data processing costs to the Federal Reserve Board.

HUD staff have also provided training on the Fair Housing Act to the headquarters and regional consumer complaint specialists of the Office of the Comptroller of the Currency.

And HUD staff have met with the Director of Consumer Compliance at the Office of Thrift Supervision to discuss possible joint investigations and cross-training on the Fair Housing Act and Community Reinvestment Act. OTS has supplied HUD with copies of its consumer compliance materials—that is, the examiner's manual and self-assessment guide—and HUD is examining these materials to see whether they would be useful in FHA's oversight of FHA-approved lenders.

We stated that we would enhance FHA insurance operations systems to provide additional information and we have done so.

We are now collecting the required HMDA data on rejected applicants, as well as approved borrowers. A mortgagee letter to all FHA-approved lenders advising them of the HMDA requirements should be issued by June 30, 1990.

And, in addition, the Department has determined that section 311 of HMDA, in conjunction with section 808 of the Fair Housing Act, permits HUD to collect and mandates HUD to disseminate data on applicants and approved borrowers for FHA insured mortgage from all originators of such mortgages, even if they are otherwise exempt from the Federal Reserve Board's regulation C reporting requirements.

Also, in accordance with our testimony last fall, we are identifying and investigating various forms of credit discrimination and steering.

In order to develop relevant measures of credit allocation by tract, race, and income, our Office of Policy Development and Research has conducted a preliminary examination of FHA lending data in nine metropolitan areas. These are attached to the testimony.

There are no clear, uniform practices or patterns to suggest that discrimination by FHA lenders is occurring in these areas, but HUD expects to continue this analysis to improve our understanding of geographic and racial patterns of FHA lending and to see if discrimination may be a problem in other areas.

COOPERATION WITH FEDERAL FINANCIAL REGULATORY AGENCIES

We have also followed through on our commitment to work closely with the Federal financial regulatory agencies and other experts and interest groups to develop practical monitoring and enforcement procedures.

In addition to our work with FFIEC and the other agencies that I've already mentioned, HUD has:

Sponsored a colloquium last November featuring Constance R. Dunham, the author of a study conducted for the Federal Reserve on geographic patterns of mortgage lending in Boston from 1982 to 1987.

We have recently sponsored a colloquium entitled "Lending: Testing for Credit Discrimination," featuring Allen Fishbein and Deborah Goldberg of the Center for Community Change and Zina Greene, author of the "Lender's Guide to Fair Lending Practices." This included a description of work done by the CCC for the Kentucky Commission on Human Rights and the New York State Division on Human Rights under HUD's Fair Housing Assistance Program.

HUD also plans to hold a credit discrimination research conference in late 1990 or early 1991. The objective will be to develop improved measures of credit discrimination and to analyze the new applicant characteristics data soon to be available under HMDA.

And finally, HUD has undertaken several additional initiatives supporting eradication of lending discrimination and aimed at increasing the supply of mortgage credit to underserved areas, which are included in the testimony.

Mr. Chairman, our ability to continue to make progress in reducing lending discrimination and redlining is dependent in a part on our ability to fully enforce the Fair Housing Act. When I testified before your full committee at my confirmation hearing on November 20, 1989, I stated that it would take 3 years for the enforcement system to be fully implemented. And as you know, the Congress enacted far-reaching amendments which went into effect on March 12, 1989.

Fiscal year 1989 was spent writing regulations, designing system standards for investigation, case processing and reporting, hiring additional staff and training. During the current fiscal year, we are refining system standards, improving investigations and report writing for quality and timeliness, hiring additional staff and doing more training. We expect our new computer system to be operational by June 30, 1990.

By late this year or early next year, we expect to have developed our standards for Secretary-initiated investigations and complaints. That timing should coincide with the availability of HMDA data on rejected applicants so that we can bring to bear the full power of the Secretary on the difficult problem of lending discrimination.

You can be assured that under the leadership of Secretary Kemp HUD will continue to report progress to you at future hearings.

I should be glad to answer any questions that you may have.

[The complete prepared statement of Gordon Mansfield follows:]

STATEMENT OF GORDON H. MANSFIELD

ASSISTANT SECRETARY FOR FAIR HOUSING AND EQUAL OPPORTUNITY
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
BEFORE THE
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

MAY 16, 1990

Chairman Dixon and members of the Subcommittee. I am Gordon H. Mansfield, HUD's Assistant Secretary for Fair Housing and Equal Opportunity, with responsibility for adminstering the Fair Housing Act, which prohibits discrimination in the sale, rental or financing of housing, and assuring that all HUD programs affirmatively further fair housing. I am accompanied today by Ron Rosenfeld, HUD's Deputy Assistant Secretary for Single-Family Housing.

The Department of Housing and Urban Development appreciates the opportunity to describe our progress in eliminating discrimination in home mortgage lending since your last hearing in October 1989.

* * * *

First, let me describe our enforcement efforts under the Fair Housing Act. Improvements to our data system since last October enable me to provide you with more detail than we did then. From October 1, 1987 to April 24, 1990, we received 342 complaints alleging lending discrimination or redlining.

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Significant settlements include:

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A $150,000 loan which had allegedly been denied by a savings and loan association based on race. The complainant could select the interest rate at the time of application or settlement.

Among the cases under investigation are:

- allegations by a midwestern builder that a local bank discriminated against him by refusing to provide loans in a predominantly minority neighborhood.

- allegations that residents of minority neighborhoods in a particular community are steered to FHA loans, rather than conventional loans, and to mortgage bankers rather than depository institutions, resulting in higher interest rates.

In addition, as data begin to flow into the Department on rejected, as well as accepted applicants, we expect to identify appropriate lenders for Secretary-initiated investigations.

* * * *

I am pleased to report that the HMDA data for all single-family FHA loans by census tract for 1980-89, which HUD is charged with making available, were delivered last week to the Federal Financial Institutions Examination Council (FFIEC). These data should be available for public use by July 15, 1990. This will fulfill Secretary Kemp's commitment, which Assistant Secretary Pitts made to this Subcommittee in October.

* * * *

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* * * *

We stated that we would enhance FHA insurance operations systems to provide additional information. We have done so.

We are now collecting required HMDA data on rejected applicants as well as approved borrowers. On a monthly basis, these data are geocoded with the required geographic information including Metropolitan Statistical Area and Census Tract. We are in the process of changing the reporting form for Title I Home Improvement Loans and Manufactured Housing Loans to provide applicant data under these programs. A mortgagee letter to all FHA approved lenders advising them of the HMDA requirements should be issued by June 30,1990.

In addition, the Department has determined that section 311 of HMDA, in conjunction with section 808 of the Fair Housing Act, permits HUD to collect--and mandates HUD to disseminate--data on applicants and approved borrowers for FHA-insured mortgages from all originators of such mortgages even if they are otherwise exempt from the Federal Reserve Board's Regulation C reporting requirements.

* * * *

In accordance with our testimony last fall, we are identifying and investigating various forms of credit discrimination and steering.

In order to develop relevant measures of credit allocation by tract, race and income, our Office of Policy Development and Research has conducted a preliminary examination of FHA lending data in nine metropolitan areas. (See tables 1 and 2). There are no clear, uniform patterns to suggest that discrimination by FHA lenders is occurring in these areas. HUD expects to continue this analysis to improve our understanding of geographic and racial patterns of FHA lending and to see if discrimination may be a problem in other areas.

* * * *

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* * * *

Finally, HUD has undertaken several additional initiatives supporting eradication of lending discrimination and aimed at increasing the supply of mortgage credit to underserved areas.

* The Assistant Secretary for Fair Housing and Equal Opportunity and the Assistant Secretary for Housing-Federal Housing Commissioner have established a Fair Housing Task Force. The Task Force is charged with reviewing and analyzing internal operations within FHA--including underwriting standards and oversight of approved mortgagees--to assure that they fully support fair housing objectives and operate affirmatively to meet community credit needs.

* HUD has launched an effort to increase availability of FHA mortgage insurance in areas that have previously been underserved. Through this FHA Greenlining Initiative, HUD plans to identify mortgagees who are willing and able to make loans in inner-city, rural, and other underserved areas, support the efforts of those mortgagees, and then replicate their results throughout the country. To this end, we have met with housing finance agencies, FNMA, the Enterprise Foundation, the Low Income Housing Fund and the AFL-CIO Housing Trust to seek their cooperation and interest and share expertise.

* In active support of the Community Reinvestment Act, HUD has recently launched the Community Development and Housing Investment Support Strategy. Implementation, which is just beginning, will involve establishing a clearinghouse of information concerning successful community investment ventures by private and public financial institutions as well as information about existing HUD programs that can be used to support community investment. HUD field offices will provide technical assistance and share this information with interested financial institutions, communities, community organizations, and other potential community investment participants. HUD hopes that this effort will expand opportunities for homeownership, and

that this effort will expand opportunities for homeownership, and provide more affordable housing, economic development and job creation.

* * * *

Mr. Chairman, our ability to continue to make progress in reducing lending discrimination and redlining is dependent, in part, on our ability to fully enforce the Fair Housing Act. When I testified before your full Committee at my confirmation hearing on November 20, 1989, I stated that it would take three years for the enforcement system to be fully implemented. As you know, the Congress enacted far-reaching amendments which went into effect on March 12, 1989.

Fiscal Year 1989 was spent writing regulations, designing system standards for investigations, case processing and reporting, hiring additional staff and training.
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By late this year or early next year we expect to have developed our standards for Secretary-initiated investigations and complaints. That timing should coincide with the availability of HMDA data on rejected applicants so we can bring to bear the full power of the Secretary on the difficult problem of lending discrimination.

You can be assured that under the leadership of Secretary Kemp HUD will continue to report progress to you at future hearings.

I should be glad to answer any questions that you may have.

Table 1

NUMBER OF FHA LOANS BETWEEN 1985-89 FOR CENSUS TRACTS OF DIFFERING RACIAL COMPOSITION
(Selected SMSAs, 1985-1989)

SMSA LOCATION AND TRACT RACIAL COMPOSITION	FHA VOLUME[1]	FHA RATE[2]	MED. LOAN TO VALUE RATIO[3]	AVER. LOAN TO VALUE RATIO[4]	AVERAGE MORTGAGE AMOUNT[5]	MEDIAN HSEHOLD INCOME[6]	AVERAGE HSEHOLD INCOME[7]
			ATLANTA, GEORGIA				
TRACTS 0-25% BLACK	56024	0.090	88.4	85.9	$66,655	$35,829	$45,102
TRACTS 25-75% BLACK	7056	0.089	90.1	87.8	$58,834	$24,409	$31,178
TRACTS OVER 75% BLACK	4317	0.060	91.0	89.0	$48,293	$16,052	$20,914
ALL TRACTS	67397	0.084	89.2	86.8	$61,693	$29,822	$37,763
			BIRMINGHAM, ALABAMA				
TRACTS 0-25% BLACK	8882	0.048	89.7	86.6	$51,892	$27,333	$32,915
TRACTS 25-75% BLACK	1666	0.061	91.5	88.6	$39,324	$19,115	$23,566
TRACTS OVER 75% BLACK	869	0.029	90.1	88.5	$37,683	$12,724	$16,725
ALL TRACTS	11417	0.046	90.1	87.4	$48,564	$22,870	$27,935
			CINCINNATI, OHIO				
TOTAL FOR CINCINNATI	17334	0.051	94.6	92.4	$51,206	$28,778	$35,265
INDIANA							
TRACTS 0-25% BLACK	105	0.010	94.6	93.4	$53,118	$28,465	$33,982
TRACTS OVER 25% BLACK	NO SUCH TRACTS						
ALL TRACTS	105	0.010	94.6	93.4	$53,118	$28,465	$33,982
KENTUCKY							
TRACTS 0-25% BLACK	2633	0.039	95.0	92.8	$48,262	$27,718	$33,128
TRACTS 25-75% BLACK	18	0.043	92.3	91.2	$41,474	$12,088	$15,477
ALL TRACTS	2651	0.039	94.9	92.7	$48,051	$27,067	$32,391
OHIO							
TRACTS 0-25% BLACK	11779	0.052	94.5	92.4	$54,328	$32,538	$39,683
TRACTS 25-75% BLACK	1959	0.075	94.7	92.2	$49,728	$24,340	$31,378
TRACTS OVER 75% BLACK	840	0.085	94.4	92.2	$44,643	$14,585	$19,470
ALL TRACTS	14578	0.055	94.5	92.3	$52,588	$29,282	$36,132
			HARTFORD, CONNECTICUT				
TRACTS 0-25% BLACK	4194	0.032	82.0	78.7	$76,392	$37,156	$45,254
TRACTS 25-75% BLACK	386	0.088	89.8	85.1	$72,272	$19,549	$25,310
TRACTS OVER 75% BLACK	212	0.061	90.3	86.6	$79,748	$20,035	$25,339
ALL TRACTS	4792	0.038	82.9	79.5	$76,211	$34,828	$42,596
			JACKSON, MISSISSIPPI				
TRACTS 0-25% BLACK	9194	0.149	89.3	86.6	$55,287	$32,825	$41,135
TRACTS 25-75% BLACK	2368	0.112	90.1	86.2	$47,454	$19,939	$25,387
TRACTS OVER 75% BLACK	1255	0.053	90.2	87.7	$42,034	$13,316	$17,822
ALL TRACTS	12817	0.109	89.8	86.9	$49,235	$23,582	$30,012
			KANSAS CITY, KANSAS				
TOTAL FOR KANSAS CITY	28703	0.064	91.5	87.3	$49,061	$29,056	$35,056
KANSAS							
TRACTS 0-25% BLACK	6452	0.042	90.7	87.1	$54,770	$35,467	$42,735
TRACTS 25-75% BLACK	473	0.043	91.5	89.1	$40,789	$21,791	$26,308
TRACTS OVER 75% BLACK	60	0.010	90.2	89.9	$30,706	$11,172	$14,908
ALL TRACTS	6985	0.039	90.8	87.6	$51,461	$31,819	$38,462
MISSOURI							
TRACTS 0-25% BLACK	18974	0.080	92.1	87.4	$51,320	$30,563	$36,469
TRACTS 25-75% BLACK	1278	0.099	91.6	86.9	$42,090	$20,648	$25,712
TRACTS OVER 75% BLACK	1466	0.056	91.1	85.9	$32,983	$16,175	$20,838
ALL TRACTS	21718	0.078	91.9	87.2	$47,762	$27,543	$33,189
			SAN ANTONIO, TEXAS				
TRACTS 0-25% BLACK	33928	0.080	91.1	87.3	$49,861	$23,410	$30,049
TRACTS 25-75% BLACK	785	0.060	90.9	88.7	$38,633	$14,565	$18,173
TRACTS OVER 75% BLACK	127	0.043	89.9	86.9	$33,269	$13,063	$16,442
ALL TRACTS	34840	0.079	91.0	87.3	$48,749	$22,731	$29,142
			SAN FRANCISCO, CALIFORNIA				
TRACTS 0-25% BLACK	996	0.003	88.0	85.5	$84,145	$41,218	$53,901
TRACTS 25-75% BLACK	109	0.004	82.7	81.7	$82,394	$24,960	$33,696
TRACTS OVER 75% BLACK	31	0.006	91.2	90.1	$85,007	$17,821	$23,333
ALL TRACTS	1136	0.003	88.4	87.8	$84,020	$39,592	$51,839

SMSA LOCATION AND TRACT RACIAL COMPOSITION	FHA VOLUME	FHA RATE	MED. LOAN TO VALUE RATIO	AVER. LOAN TO VALUE RATIO	AVERAGE MORTGAGE AMOUNT	MEDIAN HSEHOLD INCOME	AVERAGE HSEHOLD INCOME
			WASHINGTON, D.C.				
TOTAL FOR WASHINGTON, D.C.	106215	0.135	84.6	81.2	$78,290	$46,037	$58,067
DIST. OF COLUMBIA							
TRACTS 0-25% BLACK	323	0.025	75.3	73.1	$80,377	$44,534	$63,906
TRACTS 25-75% BLACK	987	0.066	86.4	82.9	$77,642	$28,798	$39,895
TRACTS OVER 75% BLACK	5857	0.129	87.8	83.3	$68,811	$27,163	$35,982
ALL TRACTS	6747	0.097	85.2	81.2	$72,254	$31,222	$42,603
MARYLAND SUBURBS							
TRACTS 0-25% BLACK	30292	0.126	82.0	79.1	$80,837	$53,910	$66,625
TRACTS 25-75% BLACK	17019	0.199	90.6	86.6	$78,671	$41,436	$51,179
TRACTS OVER 75% BLACK	3983	0.165	93.2	89.2	$73,712	$38,289	$47,683
ALL TRACTS	51294	0.154	86.0	82.5	$79,418	$48,352	$59,790
VIRGINIA SUBURBS							
TRACTS 0-25% BLACK	44944	0.129	81.7	79.0	$81,464	$54,925	$68,465
TRACTS 25-75% BLACK	3042	0.239	88.6	85.5	$73,770	$33,283	$45,555
TRACTS OVER 75% BLACK	188	0.143	84.7	79.6	$75,746	$28,648	$39,759
ALL TRACTS	48174	0.138	82.3	79.5	$80,789	$53,066	$66,330
			CITIES WITH A LARGE SPANISH POPULATION				
			SAN ANTONIO, TEXAS				
TRACTS 0-25% SPANISH	14136	0.080	87.3	84.0	$61,225	$34,978	$45,911
TRACTS 25-75% SPANISH	15905	0.093	91.8	88.0	$48,071	$21,162	$26,669
TRACTS OVER 75% SPANISH	4799	0.062	93.5	89.6	$38,690	$13,821	$17,281
ALL TRACTS	34840	0.079	91.0	87.3	$48,749	$22,731	$29,142
			SAN FRANCISCO, CALIFORNIA				
TRACTS 0-25% SPANISH	1000	0.003	68.9	65.4	$84,056	$41,041	$53,983
TRACTS 25-75% SPANISH	136	0.003	78.4	77.6	$83,869	$30,807	$38,973
TRACTS OVER 75% SPANISH	NO SUCH	TRACTS					
ALL TRACTS	1136	0.003	68.4	67.8	$84,020	$39,392	$51,889

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1. Number of mortgages endorsed for FHA insurance between 1985 and 1989.

2. The ratio of FHA loan volume between 1985-88 to the total estimated eligible single family housing units in the geographic area in 1989. The 1989 population estimates and the 1980 census information was derived from the Donnelly Corporation CONQUEST data system. The specific formula used for the calculation is as follows:

   FHA Rate=FHA Volume / $(HH^{89} * (HH^{80}/Owner^{80})$

   where FHA Volume = Mortgages endorsed for FHA insurance, 1985-89
   HH^{89} = Projected Number of Households in 1989
   HH^{80} = Number of Households in 1980
   $Owner^{80}$ = Number of Owner-occupied units in 1980

   The under projection of the estimated number of households in geographic areas with high 1980-89 growth rates, may lead to an over-estimation of FHA rates in rapidly changing census tracts of an unknown amount.

3. Median ratio of the mortgage loan amount to the estimated value of the property.

4. Average loan to value ratio.

5. Average mortgage loan amount in the census tracts of the geographic area.

6. Estimated median household income in 1989.

7. Estimated average household income in 1989.

Table 2

NUMBER OF FHA LOANS BETWEEN 1985-89 IN CENTRAL/NON-CENTRAL CITY CENSUS TRACTS
OF DIFFERING RACIAL COMPOSITION
(Selected SMSAs, 1985-1989)

SMSA LOCATION AND TRACT RACIAL COMPOSITION	FHA VOLUME[1]	FHA RATE[2]	MED. LOAN TO VALUE RATIO[3]	AVER. LOAN TO VALUE RATIO[4]	AVERAGE MORTGAGE AMOUNT[5]	MEDIAN HSHOLD INCOME[6]	AVERAGE HSHOLD INCOME[7]
ATLANTA, GEORGIA							
ALL TRACTS	67397	0.084	89.2	86.8	$61,693	$29,822	$37,763
CENTRAL CITY	3774	0.048	87.9	85.6	$56,275	$19,862	$27,182
TRACTS 0-25% BLACK	451	0.022	80.2	76.7	$74,849	$35,350	$50,369
TRACTS 25-75% BLACK	982	0.084	89.6	87.7	$61,075	$18,395	$23,993
TRACTS OVER 75% BLACK	2341	0.050	91.0	89.0	$46,371	$13,867	$18,474
NON-CENTRAL CITY	63623	0.098	89.7	87.3	$63,851	$33,979	$42,178
TRACTS 0-25% BLACK	55573	0.099	89.5	87.1	$65,579	$35,891	$44,421
TRACTS 25-75% BLACK	6074	0.092	90.3	87.9	$57,858	$27,031	$34,309
TRACTS OVER 75% BLACK	1976	0.108	91.2	89.1	$58,116	$25,887	$31,895
BIRMINGHAM, ALABAMA							
ALL TRACTS	11417	0.046	90.1	87.4	$46,564	$22,870	$27,935
CENTRAL CITY	3891	0.053	90.6	88.3	$40,419	$17,716	$22,267
TRACTS 0-25% BLACK	2110	0.073	90.1	87.3	$48,579	$25,101	$30,816
TRACTS 25-75% BLACK	1096	0.079	91.8	88.9	$36,459	$19,392	$23,530
TRACTS OVER 75% BLACK	685	0.030	90.6	88.7	$36,165	$12,197	$16,143
NON-CENTRAL CITY	7526	0.041	89.7	86.8	$50,854	$26,061	$31,445
TRACTS 0-25% BLACK	6772	0.042	89.6	86.5	$52,597	$27,869	$33,420
TRACTS 25-75% BLACK	570	0.042	91.3	88.3	$42,906	$18,818	$23,605
TRACTS OVER 75% BLACK	184	0.027	88.1	87.5	$44,031	$15,228	$19,488
CINCINNATI, OHIO							
ALL TRACTS	17334	0.051	94.6	92.4	$51,206	$28,778	$35,265
CENTRAL CITY	4528	0.062	94.5	92.1	$49,752	$21,608	$28,576
TRACTS 0-25% BLACK	2977	0.063	94.6	92.3	$51,824	$25,776	$33,607
TRACTS 25-75% BLACK	817	0.069	94.5	91.7	$49,408	$19,070	$26,300
TRACTS OVER 75% BLACK	734	0.055	94.3	92.1	$45,276	$14,073	$18,965
NON-CENTRAL CITY	12806	0.045	94.6	92.6	$51,967	$32,496	$38,734
TRACTS 0-25% BLACK	11540	0.042	94.6	92.6	$52,396	$32,898	$39,163
TRACTS 25-75% BLACK	1160	0.075	94.5	92.6	$48,367	$29,566	$34,631
TRACTS OVER 75% BLACK	106	0.058	95.9	93.0	$35,781	$22,003	$26,796
HARTFORD, CONNECTICUT							
ALL TRACTS	4792	0.038	82.9	79.5	$76,211	$34,828	$42,596
CENTRAL CITY	814	0.070	88.3	84.4	$75,857	$18,623	$24,347
TRACTS 0-25% BLACK	505	0.059	86.0	82.3	$76,935	$21,795	$28,056
TRACTS 25-75% BLACK	97	0.094	91.4	86.8	$69,360	$11,984	$16,972
TRACTS OVER 75% BLACK	212	0.061	90.3	86.6	$79,748	$20,035	$25,339
NON-CENTRAL CITY	3978	0.029	81.6	78.4	$76,343	$39,807	$47,979
TRACTS 0-25% BLACK	3689	0.027	81.4	78.2	$76,320	$39,678	$48,078
TRACTS 25-75% BLACK	289	0.073	87.2	82.4	$76,932	$37,705	$45,327
TRACTS OVER 75% BLACK	NO SUCH TRACTS						

SMSA LOCATION AND TRACT RACIAL COMPOSITION	FHA VOLUME	FHA RATE	MED. LOAN TO VALUE RATIO	AVER. LOAN TO VALUE RATIO	AVERAGE MORTGAGE AMOUNT	MEDIAN HOUSEHOLD INCOME	AVERAGE HOUSEHOLD INCOME
JACKSON, MISSISSIPPI							
ALL TRACTS	12817	0.109	89.8	86.9	$49,255	$23,582	$30,812
CENTRAL CITY	6850	0.115	90.4	88.0	$47,133	$22,854	$29,102
TRACTS 0-25% BLACK	3953	0.139	89.0	86.4	$54,127	$32,149	$40,753
TRACTS 25-75% BLACK	1779	0.164	92.8	90.1	$46,032	$20,767	$25,884
TRACTS OVER 75% BLACK	1118	0.065	90.8	86.6	$40,332	$14,310	$16,576
NON-CENTRAL CITY	5967	0.100	88.7	85.0	$52,983	$24,773	$31,981
TRACTS 0-25% BLACK	5241	0.161	89.0	86.9	$56,881	$33,700	$41,630
TRACTS 25-75% BLACK	589	0.048	87.2	81.9	$49,033	$18,938	$24,767
TRACTS OVER 75% BLACK	137	0.017	86.2	84.7	$47,984	$10,608	$15,962
KANSAS CITY, KANSAS							
ALL TRACTS	28703	0.064	91.5	87.3	$48,061	$29,087	$35,886
CENTRAL CITY	11721	0.065	91.8	87.4	$43,784	$24,809	$30,184
TRACTS 0-25% BLACK	8735	0.069	92.1	87.5	$48,308	$29,087	$35,290
TRACTS 25-75% BLACK	1460	0.075	91.9	88.0	$40,874	$20,301	$24,986
TRACTS OVER 75% BLACK	1526	0.046	90.9	86.7	$32,588	$15,082	$19,867
NON-CENTRAL CITY	16982	0.064	91.1	87.2	$58,863	$34,918	$41,474
TRACTS 0-25% BLACK	16691	0.064	91.2	87.2	$56,090	$35,074	$41,647
TRACTS 25-75% BLACK	291	0.063	88.7	86.8	$46,893	$28,449	$34,414
TRACTS OVER 75% BLACK	NO SUCH TRACTS						
SAN ANTONIO, TEXAS							
ALL TRACTS	34840	0.079	91.0	87.3	$48,749	$22,731	$29,143
CENTRAL CITY	24298	0.080	92.0	88.3	$42,417	$20,306	$26,063
TRACTS 0-25% BLACK	23386	0.083	92.1	88.2	$46,250	$20,939	$28,904
TRACTS 25-75% BLACK	785	0.060	90.9	88.7	$38,633	$14,865	$18,173
TRACTS OVER 75% BLACK	127	0.043	89.9	86.9	$33,289	$13,063	$16,642
NON-CENTRAL CITY	10542	0.073	87.8	84.1	$60,614	$31,488	$40,328
TRACTS 0-25% BLACK	10542	0.073	87.8	84.1	$60,614	$31,488	$40,328
TRACTS 25-75% BLACK	NO SUCH TRACTS						
TRACTS OVER 75% BLACK	NO SUCH TRACTS						
SAN FRANCISCO, CALIFORNIA							
ALL TRACTS	1136	0.003	68.4	67.8	$84,020	$39,898	$51,080
CENTRAL CITY	194	0.002	61.0	60.9	$86,225	$30,822	$42,305
TRACTS 0-25% BLACK	176	0.002	53.2	53.0	$87,256	$32,256	$44,607
TRACTS 25-75% BLACK	13	0.000	78.0	77.8	$82,183	$25,551	$34,840
TRACTS OVER 75% BLACK	5	0.002	89.8	90.1	$86,064	$14,883	$20,074
NON-CENTRAL CITY	942	0.005	71.5	70.7	$83,088	$46,147	$58,831
TRACTS 0-25% BLACK	820	0.004	70.2	69.5	$83,136	$48,908	$60,908
TRACTS 25-75% BLACK	96	0.016	89.7	87.6	$82,711	$22,908	$30,550
TRACTS OVER 75% BLACK	26	0.037	95.1	90.1	$81,831	$29,898	$36,370
WASHINGTON, D.C.							
ALL TRACTS	106215	0.135	84.6	81.2	$78,190	$48,037	$59,067
CENTRAL CITY	6747	0.097	88.2	81.2	$72,234	$31,222	$42,603
TRACTS 0-25% BLACK	323	0.025	75.3	73.1	$80,377	$44,534	$63,906
TRACTS 25-75% BLACK	367	0.066	86.4	82.8	$77,843	$29,798	$36,866
TRACTS OVER 75% BLACK	6057	0.129	87.8	83.3	$68,811	$27,183	$36,883
NON-CENTRAL CITY	99468	0.147	84.4	81.2	$80,089	$50,308	$62,089
TRACTS 0-25% BLACK	75236	0.128	81.9	79.0	$81,189	$54,463	$67,087
TRACTS 25-75% BLACK	20061	0.205	90.3	86.4	$77,984	$40,843	$50,362
TRACTS OVER 75% BLACK	4171	0.163	92.3	88.1	$73,944	$37,187	$46,779

AREA LOCATION AND TRACT RACIAL COMPOSITION	FHA VOLUME	FHA RATE	MED. LOAN TO VALUE RATIO	AVER. LOAN TO VALUE RATIO	AVERAGE MORTGAGE AMOUNT	MEDIAN HOUSEHOLD INCOME	AVERAGE HOUSEHOLD INCOME[7]
CITIES WITH LARGE SPANISH POPULATIONS							
SAN ANTONIO, TEXAS							
ALL TRACTS	34840	0.079	91.0	87.3	$48,749	$22,731	$29,142
CENTRAL CITY	24298	0.080	92.0	88.3	$45,417	$20,306	$26,043
TRACTS 0-25% SPANISH	11452	0.095	88.6	85.3	$58,731	$33,056	$43,326
TRACTS 25-75% SPANISH	8327	0.094	92.0	88.4	$46,056	$20,868	$26,471
TRACTS OVER 75% SPANISH	4519	0.062	93.6	89.6	$38,339	$13,722	$17,172
NON-CENTRAL CITY	10542	0.073	87.8	84.1	$60,614	$31,483	$40,328
TRACTS 0-25% SPANISH	2684	0.062	85.6	82.4	$64,318	$37,361	$49,117
TRACTS 25-75% SPANISH	7578	0.092	91.3	86.6	$55,556	$23,068	$27,431
TRACTS OVER 75% SPANISH	280	0.072	90.6	88.0	$49,742	$16,942	$20,742
SAN FRANCISCO, CALIFORNIA							
ALL TRACTS	1136	0.003	68.4	67.8	$84,020	$39,582	$51,839
CENTRAL CITY	194	0.002	61.0	60.9	$86,225	$30,822	$42,395
TRACTS 0-25% SPANISH	183	0.002	58.3	58.6	$86,214	$31,077	$43,221
TRACTS 25-75% SPANISH	11	0.001	73.2	71.5	$86,277	$29,432	$37,893
NON-CENTRAL CITY	942	0.005	71.5	70.7	$83,098	$46,147	$58,931
TRACTS 0-25% SPANISH	817	0.005	69.2	68.3	$83,132	$48,287	$61,811
TRACTS 25-75% SPANISH	125	0.005	80.3	79.9	$82,966	$32,017	$39,925

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1. Number of mortgages endorsed for FHA insurance between 1985 and 1989.

2. The ratio of FHA loan volume between 1985-88 to the total estimated eligible single family housing units in the geographic area in 1989. The 1989 population estimates and the 1980 census information was derived from the Donnelly Corporation CONQUEST data system. The specific formula used for the calculation is as follows:

   FHA Rate=FHA Volume / $(HH^{89} * (HH^{80}/Owner^{80})$

   where FHA Volume = Mortgages endorsed for FHA insurance, 1985-88
   HH^{89} = Projected Number of Households in 1989
   HH^{80} = Number of Households in 1980
   $Owner^{80}$ = Number of Owner-occupied units in 1980

   The under projection of the estimated number of households in geographic areas with high 1980-89 growth rates, may lead to an over-estimation of FHA rates in rapidly changing census tracts of an unknown amount.

3. Median ratio of the mortgage loan amount to the estimated value of the property.

4. Average loan to value ratio.

5. Average mortgage loan amount in the census tracts of the geographic area.

6. Estimated median household income in 1989.

7. Estimated average household income in 1989.

Senator **Dixon**. I thank you, Mr. Mansfield.

And before we proceed to Mr. Herrmann, may I recognize the distinguished Senator from New York State, Senator D'Amato.

Senator **D'Amato**. Well thank you, Mr. Chairman. Unfortunately I have a hearing that starts at 10 a.m. and we all have different constraints placed upon us, but I'd like to commend you, Mr. Chairman, and compliment you on your continuing attention to the problem of discrimination and housing finance. I look forward to continuing to work with you, not only in monitoring this but in any other avenues that you might think are appropriate.

I would ask that I might be permitted to submit my full statement as if read in its entirety.

STATEMENT OF SENATOR D'AMATO

Senator **D'Amato**. Mr. Chairman, I join you in welcoming our witnesses. I would also like to compliment you on your continuing attention to the problem of discrimination in housing finance. Discrimination in home mortgage lending is a terrible blot on the American landscape. It strikes at the heart of the one of the central themes of the promise that America still offers to the world.

Peoples from all over the world and all over the country have sought the opportunities that our vibrant urban economies offer. But they have encountered a very high cost of housing in recent years.

One of the primary objects of my years of work in the Housing Subcommittee of the Senate Banking Committee has been on the first-time home buyer. In this regard we must recognize that discrimination in mortgage lending is tantamont to denial of the opportunity to own a home.

I join you, Mr. Chairman, and our distinguished panel of witnesses in your efforts to reinvigorate enforcement of the laws aimed at this problem.

Senator **Dixon**. I thank the Senator from New York and I thank him for his support.

We're delighted to have Mr. Robert J. Herrmann, the Senior Deputy Comptroller for Bank Supervision Policy, OCC.

STATEMENT OF ROBERT J. HERRMANN, SENIOR DEPUTY COMPTROLLER FOR BANK SUPERVISION POLICY, OFFICE OF THE COMPTROLLER OF THE CURRENCY

Mr. **Herrmann**. Thank you, Chairman Dixon, Senator D'Amato. I'm here today on behalf of the Office of the Comptroller of the Currency to give the committee a status report on our efforts to enforce compliance with fair lending laws and regulations and, in particular, those related to mortgage lending.

My written statement, Mr. Chairman, is a detailed report of our efforts with a focus on our current supervision and findings. It also describes our data systems and how those systems augment our supervisory process. Furthermore, my written statement discusses the initiatives we have undertaken in cooperation with the other Federal financial regulatory agencies.

Rather than trying to summarize all the information from that written statement, I ask that it be submitted for the record and I'll then spend the next few minutes touching briefly on the major points.

Senator **Dixon**. And all these statements, may I say to every member of the panel, will be reproduced in full in the record.

Thank you, Mr. Herrmann.

Mr. **Herrmann**. Mr. Chairman, the OCC is committed to enforcing the spirit and letter of fair lending laws and regulations in the national banking system. The OCC's responsibility is to ensure that national banks, one, comply with the requirements of fair lending laws and, two, rectify possible patterns or practices that indicate illegal discrimination. We believe that our supervisory programs are efficient and effective in promoting compliance. We strive to insure compliance by requiring that when we find violations corrective action is taken and better systems are implemented so that violations will not recur. And we continually strive to improve our processes and supervision; a never-ending effort in this fast changing environment.

In previous testimony, we described in detail our formal compliance program and the requirement that thorough and consistent compliance exams be conducted in a statistically valid sample of national banks. Information gained from these examinations shows that national banks are implementing programs to improve their level of compliance. Virtually all national banks now have compliance officers. And we have seen the percentage of national banks with compliance management committees increase from 24 percent in 1987 to more than 36 percent currently.

But, Mr. Chairman, while we at the OCC are committed to insuring that banks comply with fair lending related legislation, we must note that illegal discrimination, particularly in mortgage lending, is very difficult to detect because it can occur at so many different stages in the process of securing mortgage financing. Activities that occur prior to a bank's receiving a written application are especially difficult to detect because there is no tangible evidence on which to rely.

In short, Mr. Chairman, the difficulties we face are significant but we are facing them, and in the process we believe we are achieving significant results.

For example, during the 3 years since the implementation of our program, the OCC has conducted almost 4,000 consumer examinations. In those examinations, we cited 140 violations of the discrimination provisions of the Equal Credit Opportunity Act and its implementing regulation, regulation B.

When banks have been cited for violating regulation B, we promptly require the institution to first correct the practice which led to the violation and, second, implement systems to insure that such violations will not recur, and, finally, correct the effects of the discovered violations. Banks found to be in violation are required to conduct file searches for the previous 2 years and initiate corrective action for each customer who was aversely affected.

And I want to stress, Mr. Chairman, that when a consumer complaint alleging illegal discrimination appears to warrant such a commitment of resources, we conduct a thorough investigation.

Mr. Chairman, my written statement goes into our activities and programs in much more detail than we have time in this opening statement. In particular, it discusses our supervisory efforts, including activities related to the Community Reinvestment Act, our preparation and continuing training of our examiners, our data systems and our involvement with other agencies and, in particular, the four projects to enhance enforcement of fair lending and community laws now being studied by the Federal Financial Institutions Examination Council. It also answers the questions you sent to us earlier.

In closing, I would again note that as bank supervisors we do have limitations in identifying incidents of fair lending discrimination, limitations that arise from the very nature of the discrimination itself. It can be subtle, it can be indirect, it can be inadvertent. But when such incidents occur, we fully realize that human beings are affected. We are sensitive to this fact and believe that as those incidents occur we have developed and constructed a strong compliance program to address them.

Thank you, Mr. Chairman.

[The complete prepared statement of Robert Herrmann follows:]

STATEMENT OF
ROBERT J. HERRMANN
SENIOR DEPUTY COMPTROLLER FOR BANK SUPERVISION POLICY
OFFICE OF THE COMPTROLLER OF THE CURRENCY
Before the
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
May 16, 1990

I am here today on behalf of the Office of the Comptroller of the Currency (OCC) for this followup hearing on mortgage lending discrimination. My statement is a status report on our efforts to enforce national banks' compliance with fair lending laws and regulations, particularly those related to mortgage lending, with a focus on our current supervisory efforts and findings. I will also explain our data systems as well and how they augment the supervisory process and the initiatives that we have undertaken in cooperation with the other federal financial regulatory agencies, through the Federal Financial Institutions Examination Council (FFIEC).

Introduction

We believe that the business of mortgage lending has changed radically over the last five years. A vast number of competitors in the financial services industry offer home mortgage loans with competitive terms and rates. The long-term dominance of thrifts in mortgage originations has eroded in recent years: in 1985, thrifts originated 44% of mortgages to purchase one to four family dwellings, banks originated 21%, and other financial servicers originated 35%. By 1989, the picture changed dramatically: originations by thrifts and other financial servicers decreased to 39% and 27%, respectively; commercial banks' share, on the other hand, increased to 35%. Commercial banks could not have increased their share of the mortgage market without having actively marketed their services to a broad customer base.

Compliance with all banking statutes, and particularly those related to preventing illegal discrimination, is an integral part of successful bank operations. As a result of our efforts, national banks' management personnel have become more sensitive to the need for systems to ensure compliance. Financial trade associations, including the American Bankers Association and the Bank Administration Institute, along with state banking associations have responded to this renewed emphasis by enhancing their compliance-related training programs.

The OCC has enhanced its training programs for examiners to ensure better understanding of the requirements of all consumer, fair lending and community related laws. Examiners are required to undertake a computer-based, self-study course on regulatory requirements and attend a two-week consumer compliance school, a significant portion of which is devoted to fair lending issues and requirements. In addition, two advanced consumer compliance seminars are conducted in Washington for experienced examiners who conduct compliance examinations and manage the compliance examination process. Issues related to fair lending and community reinvestment are discussed in detail during these sessions.

In previous testimony before this Subcommittee, we described in detail our formal Compliance Program and the requirement that thorough and consistent compliance examinations be conducted in a statistically valid sample of national banks. Information gained from these examinations shows that national banks are implementing programs to improve their level of compliance. Virtually all national banks now have compliance officers and, since the inception of the Compliance Program, we have seen the percentage of national banks with Compliance Management Committees increase from 24% in 1987 to over 36%. Our staff participates in numerous educational seminars for bankers that focus on the elements that comprise a successful compliance management program.

We also cooperate with the Department of Housing and Urban Development (HUD) in their efforts to combat illegal discrimination in housing markets. For instance, the OCC's Special Assistant for Fair Lending is a speaker at HUD's fair housing/fair lending legal seminars for attorneys and officials of lending institutions and serves as an advisor on housing discrimination related studies.

Additionally, because of the pertinent provisions of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 amending the Community Reinvestment Act (CRA) and the Home Mortgage Disclosure Act (HMDA), we, as supervisors of the national banking system, have increased pressure on bank managements to document their policies, procedures and monitoring functions. This is particularly important because compliance with anti-discrimination laws and regulations is included in two assessment factors in the CRA regulation.

The OCC is committed to ensuring that national banks comply with all fair lending-related legislation. We assert that illegal discrimination, particularly in mortgage lending, is very difficult to detect because it can occur at so many different stages in the process of securing mortgage financing. Potential customers can be affected by illegal discriminatory behavior: (1) during preliminary discussions with real estate agents, brokers, and others on where to seek financing; (2) when inquiring about mortgage loan terms with a bank's personnel; (3) at the time of filing an application with a bank; or, (4) during the bank's credit decision process.

Activities that occur prior to a bank's receiving a written application are especially difficult to monitor because there is no tangible evidence on which to rely. Nevertheless, the OCC's responsibility is to ensure that national banks: 1) comply with the requirements of fair lending laws; and 2) rectify possible patterns or practices that indicate illegal discrimination.

Supervisory Responsibilities and Efforts

The OCC carries out its responsibility to enforce fair lending laws via four primary avenues. They include:

1. Conducting thorough compliance examinations, including fair lending procedures, in institutions with over $1 billion in assets bi-annually and in a statistically valid sample of the remaining population of national banks, annually;

2. Conducting targeted examinations in national banks not included in the sample if, for instance, the supervising examiner has identified a compliance-related risk such as unsatisfactory operating procedures;

3. Analyzing every consumer complaint which alleges discrimination individually and taking appropriate follow-up action; and

4. Using information from our other supervisory information systems to facilitate fair lending supervision and encourage service of community credit needs consistent with the objectives of the Community Reinvestment Act. These systems include: Home Mortgage Disclosure Act (HMDA) Data and Fair Housing Home Loan Data System (FHHLDS) analyses.

Since the implementation of the Compliance Program in April 1987 through the end of 1989, the OCC has conducted over 1,960 compliance examinations. During the same time period, an additional 1,850 targeted consumer examinations occurred as part of our overall supervisory efforts beyond the Compliance Program sample. Of the almost 4,000 examinations we have conducted during the last three years, 140 violations of the illegal discrimination provisions of the Equal Credit Opportunity Act, and its implementing Regulation B, were cited.

When banks have been cited for violating the illegal discrimination provisions of Regulation B, the OCC takes prompt action to require institutions to: 1) correct the practice which led to the violation; 2) implement systems to ensure that such violations will not recur; and 3) correct the effects of the violations discovered. Banks found to be in violation are required to conduct file searches for the previous 24 month period (six-month period for violations involving adverse action notices) and initiate corrective action for each consumer who was adversely affected by the practice.

The OCC also integrates information from the consumer complaint process into supervision of bank compliance with law. The supervisory offices semi-annually receive bank profile reports on all banks that have been the subject of consumer complaints. The information is evaluated and, as appropriate, incorporated into the individual banks' strategies for supervision. Additionally, supervisory offices and individual examiners now have on-line access to the OCC's Consumer Complaint Information System (CCIS). Examiners analyze reports from the system and incorporate the results in the supervision of the banks.

Despite the usefulness of our automated complaint information system, the OCC continues to receive few fair lending complaints. During the three years ending March 31, 1990, the OCC received over 43,000 written complaints. Consumer complaints alleging illegal discrimination or redlining totaled 684, about 1.6% of all those received. Of these, over 400 of the complaints alleged discrimination involving credit cards. Complaints alleging racial discrimination in real estate lending totaled 37 for the three year period -- less than 0.1% of the total.

Our complaint resolution process requires that we review information submitted by the consumer and that we request the bank to provide us with its response to the allegations. Once we have reviewed all the facts pertinent to the individual complaint, we determine whether further follow-up, for instance an on-site investigation by an examiner, is necessary. Of the 37 real estate related complaints alleging racial discrimination received over the last three years and reviewed according to these procedures, we found no violations of fair lending laws.

As a result of our investigations of all other types of credit-related consumer complaints, six banks were cited for eight violations of Regulation B (the implementing regulation for the Equal Credit Opportunity Act). Two of these violations related to illegal discrimination. One violation was cited because of discrimination on the basis of marital status and the other was cited because of discrimination on the basis of receipt of public assistance income. In both cases, our investigation revealed that these were isolated errors by inexperienced loan processors and not part of a pattern or practice of illegal activity in those particular institutions. In accordance with the OCC's enforcement policy, both complainants were offered the opportunity to reapply and be reconsidered under nondiscriminatory standards.

Consumer complaints are processed by complaint specialists in each district office who receive training in all consumer protection and fair lending laws. In addition to the OCC's regular training for these laws, the most recent consumer complaint seminar, held in December 1989, also included presentations by representatives of the Department of Housing and Urban Development on the Fair Housing Act and the Federal Trade Commission on illegal discriminatory lending practices.

The complaint specialists operate with written procedures that include guidelines for processing complaints alleging illegal discrimination. Our examiners also have written guidelines for investigating complaints of illegal discrimination. We believe our complaint processing procedures are an effective tool in identifying incidents of illegal discrimination.

The OCC conducts thorough fair lending investigations when a consumer complaint alleging illegal discrimination appears to warrant such a commitment of resources. For instance, we recently received complaints about alleged discriminatory small business lending practices in two cities -- one in our Midwestern District, the other in the Southwestern District. We conducted on-site investigations in both cases. Our examiners expanded the scope of their investigation beyond evaluating the treatment of the individuals involved to include an evaluation of the fair lending practices of all major national banks in each city. Our investigations revealed no illegal discriminatory practices in any of the institutions investigated.

One of the questions included in the Chairman's April 19, 1990 invitation letter deals with the "effects test" issue. (I refer you to the response to question 3, attached, for a more detailed explanation of the "effects test".) Policies or practices legitimately designed to evaluate risk or to minimize loan processing costs may have adverse effects on groups of people, perhaps on bases prohibited by law. Perhaps the greatest challenge to our examiners in their assessment of national banks' compliance with fair lending laws is (1) to identify which of the myriad credit standards in use today may have an adverse impact on groups of people, and should adverse effects be identified, (2) to decide whether the business value of these practices could justify their use despite possible disparate impact on minorities, women, or others.

Our current approach is to evaluate and correct problems on an individual case-by-case basis while educating and sensitizing our examiners and the banks to potentially discriminatory practices. Indirect or inadvertent discrimination is often so subtle that the most effective tool against it in the long run is to increase the sensitivity of lenders and consumers alike to those practices which might lead to it.

Supervisory Systems

The OCC uses information from two other systems to facilitate fair lending supervision. These systems include the HMDA data and the Fair Housing Home Loan Data System (FHHLDS).

The changes in HMDA effected by the Financial Institutions Reform, Recovery and Enforcement Act will provide information on the disposition of applications for residential real estate loans and information about the characteristics (race or national origin, gender, and income) of applicants and borrowers. The changes also require disclosure of information about the type of purchaser of loans sold by covered institutions, and allow optional reporting of the reasons for loan denials. Financial institutions began collecting the information to be reported on January 1, 1990 and will be reporting under the new requirements no later than March 1991.

The HMDA data are useful in monitoring CRA performance, and, with the enhancements, will have some value in monitoring compliance with the Fair Housing and Equal Credit Opportunity acts. However, even with the additional reporting requirements of the HMDA amendments, an analysis of strictly HMDA data, in and of itself, will not provide sufficient information to confirm that an institution is illegally discriminating in mortgage lending.

The HMDA data and FHHLDS analyses facilitate fair lending supervision only for those banks subject to reporting requirements of the two regulations. Of the 4,350 national banks, only 2,198 were required to report housing finance activity covered by HMDA in 1989. Additionally, few banks have sufficient mortgage loan activity that might subject them to reporting requirements of the FHHLDS. In 1989, we initiated 45 analyses covering national banks with the largest home mortgage portfolios. None were found to have illegal discriminatory practices against mortgage applicants.

The FHHLDS was developed as part of the settlement reached with the National Urban League which had filed a lawsuit in 1976 against the federal financial regulatory agencies for their alleged failure to enforce the Fair Housing Act. OCC voluntarily entered into a Settlement Agreement that required the establishment of such a data collection and analysis system. The

Settlement Agreement required the retention of the system for a minimum of three years from implementation. The OCC's FHHLDS regulation became effective on January 1, 1980. We have continued to use the system since its inception, despite expiration of the Agreement.

The FHHLDS was designed as an examination tool to identify potentially discriminatory policies or practices by banks that are very active in mortgage loan originations. There have been no substantive violations of the Fair Housing Act or ECOA found as a direct result of analysis of data collected under the system. However, data collection and reporting requirements of the system are likely to be a significant deterrent to unfair lending practices.

Interagency Efforts

The OCC is working with the other financial regulatory agencies, through the FFIEC, on four projects to enhance enforcement of fair lending and community laws. These projects are being studied thoroughly to ensure that, if implemented, they will have constructive results. The four projects include:

> Executive Summary of Home Mortgage Disclosure Act Data - The Council is studying the feasibility of producing summaries of HMDA reports that will compare an individual institution's loan distribution to that of its peers in the communities in which it does business. This will provide bank managements and supervisors with an additional tool in assessing how well a community's

mortgage credit needs are being met by the institutions in that community.

Sharing Community Contact Information - The Council is pursuing the proposal to share among the participating agencies information from interviews conducted by the examining personnel with community and consumer groups. The examiners' knowledge of community credit needs would be enhanced by providing them with contact information gathered from earlier interviews. Although this would require increased coordination among the agencies, duplicative interview efforts by the participating agencies would be reduced.

Information Pamphlet - The FFIEC's Consumer Compliance Task Force is discussing the feasibility of developing a pamphlet for financial institutions and consumers. It would be used to raise the financial institutions' awareness of the existence of potential discriminatory actions and would inform consumers of their rights under the fair lending, fair housing, and community-related laws.

Mortgage Review Boards - The agencies are studying existing Mortgage Review Boards, in Boston, Philadelphia and Detroit, to determine their manner of operation and their effectiveness. Upon completion, the results of the study will be presented to the Council to determine if participation in Mortgage Review Boards should be encouraged.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) included significant amendments to the Community Reinvestment Act (CRA) of 1977. As you are aware, compliance with anti-discrimination laws is a critical aspect in an examiner's assessment of a bank's CRA performance; therefore, we believe that a discussion of CRA amendments is useful. The amendments include: (1) requiring public disclosure of an institution's CRA rating and examiners' evaluations of banks' CRA performance for examinations beginning after July 1, 1990; and (2) requiring that the Federal financial regulatory agencies provide a written evaluation of an institution's CRA performance utilizing a four-tiered descriptive rating system, in lieu of the existing five point numerical rating system.

The OCC has been working with the other Federal financial regulatory agencies through the FFIEC to implement these requirements. This has been a major undertaking, requiring hundreds of hours of staff time to draft examination guidelines and definitions of the new ratings stipulated in the amendment. This task was more formidable because of the desire by all the Federal financial regulatory agencies to develop consistent guidelines and clear definitions of the new ratings that will apply to all federally insured financial institutions.

On December 22, 1989, the FFIEC published in the Federal Register a "Notice of Request for Comment on the Uniform Interagency Community Reinvestment Act Guidelines for Disclosure of Written Evaluations and Revisions to Assessment Rating

System". Based on the 129 comments received in response to the Notice, the guidelines were revised and approved for final publication by the Council in late April. The "Uniform Interagency Community Reinvestment Act Final Guidelines for Disclosure of Written Evaluations and Revised Assessment Rating System" will be published in the Federal Register sometime this month.

Additionally, the FFIEC's Consumer Compliance Task Force retained a professional training consultant to assist in the development of the curriculum for a course on the new requirements of CRA. The training sessions are being offered this month in four locations around the country. Examiners from each of the agencies have been scheduled to attend these sessions. Over 150 experienced national bank examiners from the OCC are attending this school. They, in turn, will be responsible for training other examiners in their respective offices.

We are also finalizing the changes to our CRA-related policies, procedures, and supervisory activities to ensure that we implement the CRA amendments in the most effective, efficient and timely manner.

As mentioned earlier in this statement, FIRREA also included significant amendments to HMDA. OCC staff members have devoted significant time to working with representatives from the other financial regulatory agencies, through the FFIEC's HMDA subcommittee, to develop new HMDA disclosure statements and aggregate tables.

The OCC is also developing a computer program that will enable national banks to submit their HMDA data in machine readable form. The computer program will facilitate timely and accurate submission of data thereby improving the aggregation process. This may result in the earlier preparation of HMDA statements for individual banks and of the aggregation tables covering all financial institutions. The computer program is being designed to reduce the number of errors currently being submitted by the institutions. Thus, the processing cost will be significantly decreased.

Summary

The OCC is committed to enforcing the spirit and letter of fair lending laws and regulations in the national banking system. We believe that our supervisory programs are efficient and effective in promoting compliance. We strive to ensure compliance by requiring that corrective action is taken so that violations will not recur. Because we are aware that no system is perfect, we continue to make improvements in our processes.

Responses to Questions

1a. In how many instances over the past three years has your agency found substantive violations of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations?

As described in our statement, the OCC's Compliance Program uses a statistically valid sampling approach of the entire population of national banks. Since the implementation of the Program in April 1987 through the end of 1989, the OCC has conducted over 1,960 compliance examinations. During the same time period, an additional 1,850 targeted consumer examinations occurred as part of our overall supervisory efforts beyond the Compliance Program sample. Of the almost 4,000 examinations we have conducted during the last three years, 140 violations of the illegal discrimination provisions of the Equal Credit Opportunity Act were cited. No violations of the Fair Housing Act have been cited during this time period.

1b. Provide some examples of how these substantive violations were resolved.

When substantive violations of ECOA are identified, immediate measures are taken to correct both the conditions and practices which caused noncompliance. The Interagency Enforcement Policy for the Equal Credit Opportunity Act, attached, dictates corrective measures for specific violations of the act. We apply these actions consistently regardless of the type of illegal discrimination identified.

Examples of the types of illegal discrimination identified during our compliance examinations have included:

- Requiring more stringent credit standards for unmarried coapplicants relative to those imposed on married coapplicants;
- Requiring additional collateral for unmarried coapplicants than for similarly qualified married coapplicants; and
- Excluding applicants from consideration for credit until they reach the age of 21, even though state law enabled individuals to enter into a legally binding contract at age 18.

Generally a bank's written loan policy will not include the aforementioned illegal actions as criteria used to assess an applicant's creditworthiness. However, actual bank practices may result in patterns of adverse treatment of credit applicants prohibited by law and, thus, citations of illegal discrimination.

2. **In how many instances over the past three years has your agency referred cases of possible discrimination to the Department of Justice for prosecution? What were the results?**

Our Western District Office is currently preparing a case involving apparent illegal discrimination in the sale of other real estate owned. We have had informal contacts with the staff of the Civil Rights Division of the Department of Justice.

We have also cooperated with and assisted the Department of Justice in its investigation of real estate lending practices in Atlanta, Georgia. It is our understanding that the staff at the Department of Justice is currently analyzing the large amount of data collected as part of that investigation.

3. **Has your agency found violations of the Fair Housing Act or ECOA (Regulation B) based on an "effects test" analysis? Can you provide any specific examples of how you have used this approach to prohibit lenders from maintaining loan policies which have a discriminatory effect on minorities?**

We have not encountered violations of the Fair Housing Act or ECOA based on an effects test analysis as they relate to real estate lending. However, we have identified instances in which the effect of written or implied bank policies could have a greater adverse impact on individuals of protected classes. For example, sections of bank policies have referred to:

- The probable continuity of an applicant's employment;

- Conveyance of spousal/children's income;
- The "stability" of younger individuals; and
- Consideration of cosigners for college students.

In these instances we inform the institution that although we may not have confirmed illegal discrimination, the policies may adversely affect credit applicants on a basis prohibited by law. And even if there were extenuating circumstances in individual decisions, the overall effect of these exceptions could result in discrimination. Therefore, if these types of policies are being followed without regard to the creditworthiness of the applicant, action could be taken against the bank, including the requirement that their policies be changed, and the potential for civil liability exists.

4. How many fair lending written complaints did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation. Provide some examples of how these substantive violations were resolved.

When loan applications are denied, the applicant is advised: of the reason for the decision; that discrimination on the basis of race, sex, marital status, etc. violates the Equal Credit Opportunity Act; and the address to write if the applicant believes illegal discrimination may have been a factor in the decision. Even so, the OCC receives few fair lending complaints.

During the three years ending March 31, 1990, the OCC received about 43,000 written complaints. Approximately, 680 alleged illegal discrimination or redlining (about 1.6% of the total). Over 400 complaints alleging discrimination involved credit cards. Of the remaining 280 discrimination related consumer complaints, 37 alleged racial discrimination in real estate lending (less than 0.1% of the total).

Our written statement describes the procedures used by the complaint specialists to process and resolve consumer complaints. Utilizing these procedures, we found no violations of fair lending laws in resolving the 37 consumer complaints alleging racial discrimination in real estate lending.

As a result of our investigations of all other types of credit-related consumer complaints, six banks were cited for eight violations of Regulation B (12 CFR 202, Equal Credit Opportunity). Five of the violations were the result of inaccurate adverse action notices and one was for failure to report credit information in the name of both spouses authorized to use the account. One violation was cited because of discrimination on the basis of marital status and one violation was cited because of discrimination on the basis of receipt of public assistance income. In the two latter cases, our investigation revealed that these were errors by inexperienced loan processors and not part of a pattern or practice of illegal activity. In accordance with the OCC's enforcement policy, both complainants were offered the opportunity to reapply and be reconsidered under nondiscriminatory standards.

5. **How many fair lending telephone calls did your agency receive over the past three years? Can you characterize these inquiries? Are there any patterns among these inquiries? What are complainants told in response?**

The OCC's complaint processing staff manually records the number of telephone calls received. From April 1, 1987 through

March 31, 1990, the OCC received about 41,000 consumer complaint calls. Although, we do not have aggregate statistics on the nature of the calls received, we believe that the majority of telephone calls alleging discrimination involve credit card applications. Complainants generally are advised of the provisions of the Equal Credit Opportunity Act and provided a form to assist them in filing the complaint.

6. **Do appraisers, private mortgage insurers, or the secondary market play a role in discrimination? What should Congress do about the problem of under-appraisals of properties in minority areas? Would your agency detect this problem in its normal examination or complaint-response procedures?**

Appraisal policies and practices, mortgage insurance requirements, and other recommended underwriting guidelines of secondary market can directly affect the loan policies of institutions that originate mortgages and hence the loan decision. Many mortgage agreements are designed to meet underwriting criteria that the lender believes will facilitate sale in the secondary market.

To date, HMDA data for depository institutions show relatively little loan sale activity in areas populated by minorities. The HMDA data have been used to support the contention that secondary market underwriting guidelines have adverse effects on minority and lower-income mortgage applicants. However, HMDA data on sale of loan originations are an insufficient source of information from which to draw conclusions on whether secondary market criteria have discriminatory effects.

Mortgage brokers are more active in minority and low-income areas, than are depository institutions. Because mortgage brokers sell their loan originations, results of the analysis of the new data required by the amendments to HMDA included in the Financial Institutions Reform, Recovery, and Enforcement Act, may show that a large number of mortgages from low- and moderate-income areas are sold on the secondary market.

Generally, the secondary market has been the primary facilitator of many different types of mortgage instruments that had not existed prior to the 1980s -- including adjustable rate mortgages, graduated payment mortgages, price-level-adjusted mortgages, etc. Evidence from HUD's Mortgage Lending Survey indicates that a substantial number of loan originations during the 1980s can be attributed to the availability of these new mortgage instruments.

Different types of mortgage instruments and sale of loans to secondary market buyers are both major ways to minimize the loan originators' risks in mortgage lending. The huge growth of the secondary market and the availability of alternative types of instruments are likely to have made housing credit available to more people -- including minorities and lower-income home buyers.

A bank's board of directors is responsible for ensuring that its written lending policy includes a well-defined and effective appraisal program which also promotes compliance with anti-discrimination standards and the Fair Housing Act. The OCC's examination policies -- both for fair lending and for monitoring performance under the Community Reinvestment Act --

require review of a bank's lending policies and criteria to ensure that policies are not discriminatory either by intent or in effect. Examination procedures specifically address whether appraisal policies and other underwriting criteria are likely to be discriminatory.

However, examiners are not trained as appraisers, and would not normally attempt to reappraise an individual property that might be the subject of a consumer complaint. Both examination and consumer complaint investigation procedures would focus on overall appraisal policies and a bank's adherence to nondiscriminatory policies.

Appendix—Policy Statements
Enforcement of the Equal Credit Opportunity and Fair Housing Acts

Section 502.201.1

This document sets forth the general policies that the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency (hereafter referred to as the "agencies") will generally apply in enforcing the Equal Credit Opportunity Act and the Fair Housing Act. Coordination among the agencies is desirable to bring about uniformity in the administrative actions that will be taken when violations of the acts are detected. The Federal Home Loan Bank Board has elected not to participate in this joint policy statement because it believes its existing policies are both sufficient and compatible with the joint statement.

Supplementary Information. The following enforcement policy statement is issued pursuant to the enforcing agencies authority under the Equal Credit Opportunity Act (ECOA) (15 USC 1691, et seq.), the Fair Housing Act (42 USC 3601, et seq.); and under 8(b) of the Federal Deposit Insurance Act (12 USC 1818(b)) for the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; and under the Federal Credit Union Act (12 USC 1786(e) (1)) for the National Credit Union Administration.

The agencies believe it appropriate to remind institutions of their responsibilities under these laws and that the agencies will vigorously enforce them. Creditors will be required to institute procedures to assure that all violations of the acts, including those not cited in this policy statement, will not recur. In addition, failure to comply with certain specific provisions of the acts has been judged by the agencies to be particularly serious and usually to warrant retrospective action to correct the condition resulting from the violations.

Equal Credit Opportunity and Fair Housing Acts Enforcement Policy Statement. This enforcement policy statement ensures that the rights of credit applicants are protected by requiring creditors to take corrective action for certain, more serious past violations of the Equal Credit Opportunity and Fair Housing Acts as well as to be in compliance in the future. In an effort to achieve that objective, the agencies will encourage voluntary correction and compliance with the acts. Whenever violations addressed by this policy statement are discovered, the creditor will be required to take action to ensure that such violations will not recur and to correct the effects of violations discovered.

The agencies will generally require the creditor to take action to correct conditions resulting from violations occurring within 24 months prior to the discovery of violations by an agency. An exception is violations concerning adverse action notices for which corrective action will be required for violations occurring within six months prior to discovery.

Violations in the following areas are considered serious by the agencies and will usually be subject to retrospective corrective action:

- Discouraging applicants on a prohibited basis in violation of the Fair Housing Act or 202.4 or 202.5(a) of Regulation B.
- Using credit criteria in a discriminatory manner in evaluating applications in violation of the Fair Housing Act or 202.4 through 202.7 of Regulation B.
- Imposing different terms on a prohibited basis in violation of the Fair Housing Act or 202.4 or 202.6(b) of Regulation B.
- Requiring cosigners, guarantors or the like on a prohibited basis in violation of 202.7(d) of Regulation B.
- Failing to furnish separate credit histories as required by 202.10 of Regulation B.
- Failing to provide an adequate notice of adverse action under 202.9 of Regulation B.

This policy statement will not:

- Preclude the use of any administrative authority that any of the agencies possess to enforce these laws.
- Limit the agencies' discretion to take other action to correct conditions resulting from violations of these laws.
- Preclude referral of cases to the Attorney General.
- Foreclose a credit applicant's right to bring civil action under the Equal Credit Opportunity or Fair Housing Acts or to file a complaint with the Department of Justice or the Department of Housing and Urban Development for violations of housing laws.
- Supersede or substitute for any regulations or enforcement policies issued by any of the agencies or the Department of Housing and Urban Development under the Fair Housing Act.

Appendix—Policy Statements

Supplementary Enforcement Policy for the Equal Credit Opportunity and the Fair Housing Acts

Part I

This document supplements and expands upon the Equal Credit Opportunity and Fair Housing Acts (the "acts") Enforcement Policy Statement recommended by the Federal Financial Institutions Examination Council (FFIEC) on September 10, 1981 and adopted by the Comptroller of the Currency.

The policy statement was issued to national banks to remind them of the seriousness of certain violations of the acts and to inform them that such violations will be dealt with by the agency retrospectively as well as prospectively. This document provides guidance by describing various actions for correcting the following substantive violations:

- Discouraging applicants on a prohibited basis.
- Using credit criteria in a discriminatory manner in evaluating applications.
- Imposing different terms on a prohibited basis.
- Requiring cosigners, guarantors and the like, on a prohibited basis.
- Failing to maintain and furnish separate credit histories.
- Failing to provide proper adverse action notification.

The OCC generally will use those actions described in Part II of this document, as appropriate, to correct the conditions caused by the violation. However, if the OCC believes that different corrective action would be more suitable, this policy does not preclude our discretion to use it.

This policy provides guidance for correcting both the conditions and practices resulting from violations of the acts. When violations of the acts addressed by the policy statement are discovered, the institution should be required to adopt a written compliance program to ensure that they will not recur. The program normally should include employee training in the requirements of the acts and the establishment of an internal controls program. The institution may be required to include a written loan policy or written appraisal standards in the compliance program should the violations of the acts so warrant.

Part III of this document contains three examples of how this policy might be implemented.

Part II

1. *Discouraging Applicants on a Prohibited Basis in Violation of the Fair Housing Act, or Section 202.4 or 202.5(a) of Regulation B.*

When this violation is discovered, the institution should be directed to adopt, in consultation with the enforcing agency, a program to reverse and overcome the effects of those practices by the institution that have limited participation in its credit programs by the discouraged group.

Each program normally should be tailor-made and designed to increase applications from the discouraged group.

The program should include an in-house training program and such marketing techniques as are necessary to encourage or solicit applications from the discouraged groups. Among the techniques that have proven successful are:

- Advertising in appropriate media, particularly through the depiction of members of the discouraged group as successful applicants.
- Establishing new business relationships with real estate brokers, automobile dealers, or other arrangers of credit who generally service the discouraged group.
- Sending direct mailings to members of disfavored classes.
- Contacting representative community groups to be employed in the credit evaluating process.
- Sponsoring credit education programs.

If specific individuals have been identified who have been discouraged on a prohibited basis from applying for credit, the institution should be required to send to all such discouraged applicants a notice that contains:

- The solicitation of a (new) application.
- A disclosure that the applicant has 60 days in which to (re) apply.

2. *Using Credit Criteria in a Discriminatory Manner in Evaluating Applications in Violation of the Fair Housing Act or Sections 202.4 through 202.7 of Regulation B.*

When this violation is discovered, the institution should be required to identify all applicants affected by the discriminatory standard(s) within the 24-month period prior to discovery of the violation by the enforcing agency.

These applicants will be sent a notice that includes:

- The solicitation of a new application by the institution.
- Disclosure that the applicant has 60 days in which to reapply.
- A description of the conditions under which any refund or reimbursement will be made.

In addition to the above customer notification requirements, the institution should be instructed to notify any party it previously informed of the rejection and inform that party to correct the applicant's credit history by deleting the previously reported rejection.

The institution should be required to offer to refund any fees or costs associated with submitting or processing the original application in the notice. This refund offer should include, at a minimum, application, appraisal, prepaid, and credit check fees. Upon re-application, the institution should not be allowed to require applicants to pay fees or costs associated with submitting or processing the new application. Such fees may be charged, however, if the application is approved. The sum of those fees must be the lesser of the total in effect at the time of original application.

In evaluating borrowers' applications, the institution should be directed to use the creditworthiness standards in effect at the time of the original applications, absent any discriminatory elements, or those currently in effect, whichever are more favorable to an applicant.

If the new applications are approved and are for credit other than open-end, the terms offered will be those currently in effect or those in effect at the time of the original applications, whichever the agency deems most appropriate.

If applicants reapply and new applications are approved, but the applicants have obtained alternative credit in lieu of that denied on a prohibited basis, the agency will consider requiring the creditor to refund fees and costs required by subsequent creditors to pay off the alternative credits. For applicants who have not obtained alternative credit, the agency should require that the costs for submitting and processing new approved applications will be the lesser of the total currently being charged by the institution on the total in effect at the time of the original applications.

The institution should be allowed to terminate the reapplication offer if it does not receive a reapplication within 60 days.

3. *Imposing More Onerous Terms on a Prohibited Basis in Violation of the Fair Housing Act or Section 202.4 or 202.6(b) of Regulation B.*

When this violation is discovered, the institution should be required to identify all such loans and notify consumers within 60 days of the corrective action. The institution should be required to offer to substitute nondiscriminatory terms for any terms illegally required and reimburse applicants for any money illegally required.

When the institution has improperly imposed a higher annual percentage rate, higher finance charges, insurance, or other loan fees, such as points on a real estate loan, the institution should be instructed to reimburse consumers the money illegally required.

When the institution has imposed other more onerous terms, such as requiring higher downpayments, shorter maturities, or stricter collateral requirements, it should be instructed to offer to change the account from the terms illegally required to the terms for which applicants should have qualified. The institution should be instructed that no fees for processing such changes may be assessed, and that the offers must state that fact.

The method for reimbursement to applicants should be the lump sum or the lump sum/payment reduction method, at the institution's option. In the case of a loan which is in default, the institution should be instructed to reduce the balance with any monies illegally required.

4. *Requiring Cosigners on a Prohibited Basis in Violation of Section 202.7(d) of Regulation B.*

When this violation is discovered, the institution should be instructed to identify all affected applicants and release additional parties where appropriate. The institution should be instructed to absorb any cost associated with the illegal requirements, such as recording or filing fees, or fees for consumer reports, imposed on applicants by the institution or by any third party in connection with the illegal requirement.

If an applicant was individually creditworthy, but a cosigner, guarantor, or other additional party was required in violation of the act, the institution should be directed to notify all parties that the additional party will be released unless other instructions are received within 30 days from the parties to the debt. The notice of release should be sent to all contractually liable parties.

If an additional party was necessary to support the extension of credit requested, but the institution restricted the applicant's choice of parties on a prohibited basis, the institution should be directed to include in the notice sent to all parties that the applicant may substitute a creditworthy party to provide the necessary support to maintain the extension of credit. The notice also should state that the additional party originally required will be informed of the effective date of the release, provided a suitable substitute is found. The institution should be instructed that the offer to accept another party should remain in effect for at least 60 days. If an applicant was individually creditworthy, but was rejected because of inability or unwillingness to furnish a cosigner, guarantor, or other additional party required by the institution in violation of the act, the appropriate remedy is provided in No. 2 above.

If an additional party was necessary to support the extension of credit requested, and the applicant offered a financially responsible party but was rejected because of inability or unwillingness to furnish an alternative party or particular additional party specified by the institution in violation of the act, the appropriate remedy also is provided in No. 2 above. If any changes to the account are made regarding the cosigner, guarantor, or other additional parties, the institution should be directed to report them to the appropriate consumer reporting agency.

5. *Failing to Furnish Separate Credit Histories for Married Persons in Violation of Section 202.10 of Regulation B.*

When this violation is discovered, the institution should be instructed to identify all affected applicants and take the following corrective actions as appropriate within 30 days: (1) designate joint accounts to reflect the participation of both spouses and comply with the requirements of section 202.10(a)(2) and (3); (2) notify consumer reporting agencies to which it has furnished credit information of the separate credit histories improperly or inaccurately and request them to amend their records to reflect such histories properly; and (3) notify the account holder that this information was not reported accurately, that it may have been the cause of a credit denial from other creditors, and that if credit was denied on the basis of an insufficient or nonexistent credit history or credit file, the applicant may want to reapply.

If the institution has failed to obtain sufficient information for accounts held by married persons, the institution should be directed to request the necessary information it lacks within 30 days.

Upon receipt of the information, the institution should be instructed to take the reporting and notification actions specified in the preceding paragraph.

6. *Failing to Provide Notices of Adverse Action in Violation of Section 202.9 of Regulation B.*

If the institution has failed to send notices of adverse action to applicants against whom adverse action has been taken, the institution should be directed to identify such applicants and send adequate adverse action notices.

If the institution has failed to provide an adequate notice of adverse action or has failed to provide an accurate statement of the reasons for denial to applicants against whom adverse action has been taken, the institution should be directed to send an adequate adverse action notice to all affected applicants.

The corrective action time period for violations of this section is six months prior to the discovery of the violation.

Part III

The following case studies illustrate the application of the foregoing corrective actions to specific situations.

Case I:

The examination revealed that some, but not all, loans to minority groups were made with more onerous terms than the creditor's average loan for any given time period. These applications were submitted to the loan committee with a stated rate of ¼ point above those for nonminorities. In five cases, the applications involved an extra point, upon the recommendation of the loan officer.

These loans were traced to two of the creditor's 12 loan officers. Both worked in the same branch office. The examiner reported that the creditor received few applications from minorities living in the area served by the branch.

1. To prevent recurrence of the violation, the agency required the creditor to:
   - Sign a written agreement that described the violations and specified the corrective action the creditor would take.
   - Issue a memorandum to employees describing the problem and directing that loan applications should be taken for the same terms, regardless of the identity of the applicant(s).
   - Revise the written underwriting standards to incorporate the instructions issued in the memorandum above.
   - The agency further required the creditor to conduct training for all loan officers to assure that they are familiar with the acts and with the creditor's nondiscriminatory underwriting policies.
2. Because this practice, limited to one branch, may have presented a discriminatory impression to the area served by the branch, the agency also required the creditor to take the following actions to correct this preception.
   - Place advertisements, including the current terms at which credit is available, in local newspapers, especially any having circulation in the community served by the branch, that solicit applications for credit.
   - Inform real estate brokers who regularly deal with the adversely affected groups of the lender's credit and underwriting standards.
   - Conduct a credit education course in the community to include information on how to qualify for credit and how to prepare a credit application.
3. To correct conditions caused by the violation, the agency required the creditor to:

- Identify the individuals affected by this policy and advise them that their rates were adjusted.
- Correct the loan contracts to eliminate the higher interest rate, with no charge to the borrowers for this action.
- Reimburse the five individuals for the extra point they had been charged and refund the overcharges resulting from higher interest rate.

Case II:

The examination showed that the creditor required cosigners of all single applicants for car loans without regard to whether or not the individual met the creditor's credit standards without the cosigner. The creditor's written instruction to loan officers did not mention cosigners or the circumstances in which one would be required.

1. To prevent recurrence of the violation, the agency required the lender to:
   - Sign a written agreement that described the violation and the corrective action the lender would take.
   - Circulate a memorandum to all employees advising them of the revised procedure.
   - Amend the written procedures to provide instructions on how single applicants are to be evaluated and when cosigners should be requested, consistent with the acts.
   - Conduct a half-day staff meeting with all loan processors to discuss evaluation of applicants under the acts and how the new procedures apply.
2. To notify the public of the current nondiscriminatory practice, the agency required the creditor to:
   - Direct several advertisements toward single individuals with the message that they can qualify for credit without a cosigner.
3. To correct the conditions caused by the violation, the agency required the creditor to:
   - Remove any illegally required cosigner, or, if a cosigner was needed, offer to allow the borrower to substitute a qualified cosigner of his or her choice.

Case III

The examiner reported that the creditor converted all applications for charge cards to the name of the male applicant and filed and reported the credit history under his name only. Women had to request their credit history under the male co-owner's name.

1. The agency required the creditor to take the following action to prevent the violation from recurring:
   - Sign a written agreement that identified the violation and specified the corrective action the creditor would take.
   - Revise all instructions to employees correcting the procedures for reviewing, recording, and reporting credit.
   - Develop new written procedures for processing credit applications.
2. To correct the conditions caused by the creditor's practice, the agency required the lender to:
   - Identify all affected individuals and notify them of the changes that would be made to their accounts to correct the violation, including an offer to change the names in which the account was held.
   - Notify affected account holders that the information reported incorrectly may have been the cause of a credit denial based on insufficient credit history and advise those individuals that they may wish to reapply.
   - Notify consumer reporting services of the changes, requesting them to correct the credit history.
3. To assure compliance, the agency should schedule a special limited examination after six months to review the creditor's progress under the corrective action agreement.

STATEMENT OF
ROBERT J. HERRMANN
SENIOR DEPUTY COMPTROLLER FOR BANK SUPERVISION POLICY
OFFICE OF THE COMPTROLLER OF THE CURRENCY
Before the
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
May 16, 1990

Summary of Statement

Introduction

The OCC has enhanced its training programs for examiners to ensure better understanding of the requirements of all consumer, fair lending and community related laws. Examiners are required to undertake a computer-based, self-study course on regulatory requirements and attend a two-week consumer compliance school, a significant portion of which is devoted to fair lending issues and requirements. In addition, two advanced consumer compliance seminars are conducted in Washington for experienced examiners who conduct compliance examinations and manage the compliance examination process. Issues related to fair lending and community reinvestment are discussed in detail during these sessions.

Additionally, we, as supervisors of the national banking system, have increased pressure on bank managements to document their policies, procedures and monitoring functions. This is particularly important because compliance with anti-discrimination laws and regulations is included in two assessment factors in the CRA regulation.

The OCC is committed to ensuring that national banks comply with all fair lending-related legislation. The OCC's responsibility is to ensure that national banks: 1) comply with the requirements of fair lending laws; and 2) rectify possible patterns or practices that indicate illegal discrimination.

Supervisory Responsibilities and Efforts

The OCC carries out its responsibility to enforce fair lending laws via four primary avenues. They include:

1. Conducting thorough compliance examinations, including fair lending procedures, in institutions with over $1 billion in assets bi-annually and in a statistically valid sample of the remaining population of national banks, annually;
2. Conducting targeted examinations in national banks not included in the sample if, for instance, the supervising examiner has identified a compliance-related risk such as unsatisfactory operating procedures;
3. Analyzing every consumer complaint which alleges discrimination individually and taking appropriate follow-up action; and
4. Using information from our other supervisory information systems to facilitate fair lending supervision and encourage service of community credit needs consistent with the objectives of the Community

Reinvestment Act. These systems include: Home Mortgage Disclosure Act (HMDA) Data and Fair Housing Home Loan Data System (FHHLDS) analyses.

Of the almost 4,000 consumer compliance examinations we have conducted during the last three years, 140 violations of the illegal discrimination provisions of the Equal Credit Opportunity Act, and its implementing Regulation B, were cited. When banks have been cited for violating the illegal discrimination provisions of Regulation B, the OCC takes prompt action to require institutions to: 1) correct the practice which led to the violation; 2) implement systems to ensure that such violations will not recur; and 3) correct the effects of the violations discovered. Banks found to be in violation are required to conduct file searches for the previous 24 month period (six-month period for violations involving adverse action notices) and initiate corrective action for each consumer who was adversely affected by the practice.

The OCC also integrates information from the consumer complaint process into supervision of bank compliance with law and conducts thorough fair lending investigations when a consumer complaint alleging illegal discrimination appears to warrant such a commitment of resources. For instance, we recently received complaints about alleged discriminatory small business lending practices in two cities. We conducted on-site investigations in both cases. Our examiners expanded the scope of their investigation beyond evaluating the treatment of the individuals involved to include an evaluation of the fair lending practices of all major national banks in each city. Our investigations revealed no illegal discriminatory practices in any of the institutions investigated.

Supervisory Systems

The OCC uses information from two other systems to facilitate fair lending supervision. These systems include the HMDA data and the Fair Housing Home Loan Data System (FHHLDS).

The changes in HMDA effected by the Financial Institutions Reform, Recovery and Enforcement Act will provide information on the disposition of applications for residential real estate loans and information about the characteristics (race or national origin, gender, and income) of applicants and borrowers. The changes also require disclosure of information about the type of purchaser of loans sold by covered institutions, and allow optional reporting of the reasons for loan denials. Financial institutions began collecting the information to be reported on January 1, 1990 and will be reporting under the new requirements no later than March 1991.

The FHHLDS was designed as an examination tool to identify potentially discriminatory policies or practices by banks that are very active in mortgage loan originations. There have been no substantive violations of the Fair Housing Act or ECOA found as a direct result of analysis of data collected under the system. However, data collection and reporting requirements of the system are likely to be a significant deterrent to unfair lending practices.

Interagency Efforts

The OCC is working with the other financial regulatory agencies, through the FFIEC, on four projects to enhance enforcement of fair lending and community laws. These projects are being studied thoroughly to ensure that, if implemented, they will have constructive results. The four projects include:

> **Executive Summary of Home Mortgage Disclosure Act Data** - The Council is studying the feasibility of producing summaries of HMDA reports that will compare an individual institution's loan distribution to that of its peers in the communities in which it does business. This will provide bank managements and supervisors with an additional tool in assessing how well a community's mortgage credit needs are being met by the institutions in that community.
>
> **Sharing Community Contact Information** - The Council is pursuing the proposal to share among the participating agencies information from interviews conducted by the examining personnel with community and consumer groups. The examiners' knowledge of community credit needs would be enhanced by providing them with contact information gathered from earlier interviews. Although this would require increased coordination among the agencies, duplicative interview efforts by the participating agencies would be reduced.
>
> **Information Pamphlet** - The FFIEC's Consumer Compliance Task Force is discussing the feasibility of developing a pamphlet for financial institutions and consumers. It would be used to raise the financial institutions' awareness of the existence of potential discriminatory actions and would inform consumers of their rights under the fair lending, fair housing, and community-related laws.
>
> **Mortgage Review Boards** - The agencies are studying existing Mortgage Review Boards, in Boston, Philadelphia and Detroit, to determine their manner of operation and their effectiveness. Upon completion, the results of the study will be presented to the Council to determine if participation in Mortgage Review Boards should be encouraged.

Summary

The OCC is committed to enforcing the spirit and letter of fair lending laws and regulations in the national banking system. We believe that our supervisory programs are efficient and effective in promoting compliance. We strive to ensure compliance by requiring that corrective action is taken so that violations will not recur. Because we are aware that no system is perfect, we continue to make improvements in our processes.

Senator DIXON. I thank you very much, Mr. Herrmann.

Mr. Bovenzi, the Deputy to the Chairman of the Federal Deposit Insurance Corporation.

STATEMENT OF JOHN F. BOVENZI, DEPUTY TO THE CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. BOVENZI. Thank you, Chairman Dixon.

I'm pleased to be here today on behalf of the Federal Deposit Insurance Corporation to testify on our activities in dealing with mortgage discrimination.

Over the past year, the FDIC has given significant consideration to additional ways in which we can further enhance the monitoring and enforcement of antidiscrimination laws. To that end we have made a number of changes in our consumer compliance program.

First, we have established a new Community Affairs Program that we believe will strengthen our efforts in the area of community outreach. The new program provides for a Community Affairs Officer in each of our eight regional offices. These officers will report to a Deputy Director in the Office of Consumer Affairs in Washington, which will have oversight responsibilities for the entire program.

The Community Affairs Officers will be responsible primarily for making contact with consumer and community groups, government and industry organizations and others regarding community needs and the lending practices of institutions within their communities. They also will be involved in formulating community lending and income profiles and performing related data analysis.

These individuals will work independently of our consumer compliance examiners; thus, they will be supplementing analyses done during the examination process. They will provide information to the examination staff to assist them in evaluating the fair lending performance of FDIC-supervised institutions. The FDIC will share the results of these efforts with other Federal financial institution regulators.

Second, the FDIC has decided to establish a new compliance examination program with specialized consumer compliance examiners. Our compliance examiners will have career paths distinct from safety and soundness examiners. The program will include an expanded corps of field compliance examiners and an increased emphasis on consumer compliance in both our Washington and regional offices.

The program will be under the jurisdiction of our Division of Supervision, but will be separate and apart from its safety and soundness examination activities. In the Washington office, we have designated an Assistant Director with particular responsibility for the new consumer compliance examination program. Further, we will soon designate in each of our regional offices an assistant regional director with specific consumer compliance responsibilities.

This new consumer compliance examination program is a significant undertaking. We plan to start phasing it in on June 30 of this year. During the phase-in, we will continue our existing practice as necessary of using examiners with both consumer compliance and safety and soundness expertise to assist in carrying out our program.

Third, the FDIC has also taken steps to strengthen its consumer compliance training program. In April 1990 we held two 1-week sessions of our newly developed Advanced Consumer Protection School. Approximately 1½ days were devoted to fair lending issues. As part of our efforts to present a balanced view on these issues, we included in the training program a presentation by Mr. Allen Fishbein, general counsel of the Center for Community Change. The Advanced Consumer Protection School will be an on-going training program. We have two additional sessions scheduled for 1990.

We are also in the process of revamping our Basic Consumer Protection School to improve its effectiveness. In connection with the development of a separate compliance examination program, we expect to further expand our training efforts. We plan to hold more frequent training sessions and to add training programs at both the Washington and regional offices.

The FDIC also intends to continue conducting consumer compliance seminars for banking in various parts of the country at which the CRA and other consumer laws and regulations are addressed. These seminars have been well attended in the past and we expect to hold at least three this year.

During the past few months, the FDIC staff has been actively involved with the other banking agencies in implementing the amendments to the CRA and HMDA contained in the Financial Institutions Reform, Recovery and Enforcement Act of 1989. We have coordinated the development of guidelines, revised regulations and examination procedures, reporting requirements and a training program.

Due to the fact that the new reporting requirements became effective so recently, it is too early to start drawing conclusions until we start receiving the data early next year. However, as our examiners conduct investigations this year, they will take into account information reflected on the new HMDA register that's now required to be maintained.

In conclusion, Mr. Chairman, Senator Bond, the FDIC continues to share the subcommittee's concerns about mortgage discrimination. We are committed to doing our part to insure that financial institutions do not engage in this illegal practice. Over the past 6 months, we have made a number of significant changes in our consumer compliance program with the goal of improving its effectiveness. These changes include new efforts at community outreach, a new consumer compliance examination program separate from the safety and soundness program, and increased consumer protection training efforts. We believe that these changes will improve our effectiveness in conducting a consumer compliance program.

That concludes my oral presentation, Mr. Chairman, and I'd be happy to answer any questions.

[The complete prepared statement of John Bovenzi follows:]

TESTIMONY OF

JOHN F. BOVENZI
DEPUTY TO THE CHAIRMAN
FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C.

ON

MORTGAGE DISCRIMINATION

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

9:30 AM
MAY 16, 1990
Room SD-538, Dirksen Senate Office Building

Good morning, Mr. Chairman and Members of the Subcommittee. The Federal Deposit Insurance Corporation is pleased to testify today on our activities in dealing with mortgage discrimination.

Over the past year, and the last six months in particular, the FDIC has given significant consideration to additional ways in which we can further enhance the monitoring and enforcement of anti-discrimination laws. To that end, we have made a number of changes in our consumer compliance programs.

Community Affairs Officers

First, we have established a new Community Affairs program that we believe will strengthen our efforts in the area of community outreach. The new program provides for a Community Affairs Officer (CAO) in each of our eight Regional Offices. These CAO's will report to a Deputy Director in the Office of Consumer Affairs in Washington, which will have oversight responsibilities for the program. The Deputy Director and CAO positions have been posted and the selection process is underway. The CAO's will be responsible primarily for making contact and meeting with consumer and community groups, government and industry organizations, and others regarding community needs and the lending practices of institutions within their communities. The CAO's also will be involved in formulating community lending and income profiles and performing related data analyses. These individuals will work independently of our compliance examiners and thus will be supplementing analyses done during the examination process. They will provide information and data to the examination staff to assist them in evaluating FDIC-supervised institutions as to their fair lending performance. The FDIC will share the results of these efforts to gather and analyze pertinent information regarding community credit needs and loan discrimination with other federal financial institution regulators.

Specialized Compliance Examiners

Second, the FDIC has decided to establish a new consumer compliance examination program with specialized consumer compliance examiners who have career paths distinct from safety and soundness examiners. The program will include an expanded corps of field compliance examiners and an increased emphasis on the consumer compliance area in both our Washington and Regional offices. The program will be under the jurisdiction of our Division of Supervision (DOS), but will be separate and apart from its safety and soundness examination activities. In the Washington Office, we have designated a DOS Assistant Director with specific responsibility for the new consumer compliance examination program. Further, we will soon designate an Assistant Regional Director with specific consumer compliance responsibilities in each of our Regional Offices.

This new consumer compliance examination program is a significant undertaking. We expect to start phasing it in by June 30 of this year. During the phase-in, we will continue our practice of using existing examiners, who have both consumer compliance and safety and soundness expertise, to assist in carrying out our compliance examination program.

Compliance Training and Education

Third, the FDIC also has taken steps to strengthen its consumer compliance training program. In April, 1990, we held two one-week sessions of our newly developed Advanced Consumer Protection School. Approximately one and a half days were devoted to fair lending issues. As part of our efforts to present a balanced view of these issues, one segment included a presentation by Mr. Allen J. Fishbein, General Counsel of the Center for Community Change. The Advanced Consumer Protection School will be an on-going training program. We have two additional sessions already scheduled for 1990. We are also in the process of revamping our Basic Consumer Protection School to improve its effectiveness. In connection with the development of the separate compliance examination program, we expect to further expand our training efforts. We plan to hold more frequent training sessions and to add training programs at both the Washington and Regional Office levels to supplement the Basic and Advanced training programs.

The FDIC also intends to continue conducting consumer compliance seminars for bankers in various part of the country, at which the Community Reinvestment Act (CRA) and other consumer laws and regulations are addressed. These seminars have been well attended in the past, and we expect to hold at least three such seminars this year.

CRA and HMDA Implementation

During the past few months, the FDIC staff has been actively involved with the other banking agencies in implementing the amendments to the CRA and the Home Mortgage Disclosure Act (HMDA) contained in the Financial Institutions Reform, Recover and Enforcement Act of 1989 (FIRREA). We have coordinated the development of guidelines, revised regulations and examination procedures, reporting requirements, and a training program.

Community Reinvestment Act

On December 22, 1989, the Federal Financial Institutions Examination Council (FFIEC) published in the Federal Register a Notice of Request for Comments on its proposal to implement changes to the CRA rating system mandated by FIRREA. The notice also set out proposed uniform procedures for disclosure of the

CRA rating and the preparation of standard, written evaluations using the twelve assessment factors for judging CRA performance. On April 20, 1990, the FFIEC approved for publication in the Federal Register the "Uniform Interagency CRA Final Guidelines for Disclosure of Written Evaluations and Revised Assessment Rating System." On April 30, the FDIC's Board of Directors approved changes to our CRA regulations (Part 345) in order to implement the FFIEC guidelines for the institutions we supervise.

From May 1 through June 1, 1990, the FFIEC is conducting interagency CRA training of examiners. The training focuses on the new CRA Assessment Rating System and Public Disclosure Guidelines. Uniformity and consistency among the agencies in evaluating institutions and assigning CRA ratings is one goal of this interagency training effort. A total of eight sessions will be held in four locations throughout the country (Atlanta, San Francisco, Pittsburgh, and Dallas). We anticipate that FDIC examiners attending the training sessions will be involved in further training in their respective Regions. The FFIEC Consumer Compliance Task Force is also developing a pamphlet for financial institutions that will address the new rating system and disclosure guidelines.

Home Mortgage Disclosure Act

Beginning this year, HMDA requires disclosure by financial institutions of both (1) data on loan applications and their disposition and (2) the race, sex and income of borrowers and applicants. The Federal Reserve Board's Regulation C, which implements HMDA, has been revised to incorporate these new requirements. These revisions require a "register" form of reporting called the Loan Application Register or "LAR" under which lenders record the required data on a loan-by-loan and application-by-application basis. Lenders began using these forms as of January 1, 1990. As provided in FIRREA, these registers will be submitted to the federal supervisory agencies in early 1991, and reports reflecting individual institution and aggregate data will then be generated.

The LAR information now required to be maintained by institutions subject to HMDA will reveal very specific data about their lending patterns. We envision that this information will help the institution determine its own mortgage profile and decide what corrective actions need to be taken to remedy any possible existing discrimination even before a regulatory agency performs its fair housing lending analysis during compliance examinations. In the past, institutions were only required to organize the volume and dollar amount of their mortgage and home improvement loans by census tract. Now the LAR data will show actual loan demand and racial, gender, and income characteristics of all applicants for such loans. The FFIEC ultimately will provide tables to institutions cross-tabulating the LAR data and enabling them to compare their individual data to the aggregate data of other institutions in their

Metropolitan Statistical Area. Even before that time, however, the institutions themselves will be in a position to recognize lending problems and perform the necessary outreach to applicants from segments of their lending areas either represented on the LAR as unsuccessful or not represented at all.

Institutions with assets under $30 million currently are exempt under HMDA from recording information about the race, sex, and income of loan applicants. To expand the opportunity for self-analysis to those institutions, the FDIC is currently working on a proposal to amend its own fair housing regulations to require these institutions to maintain that information on the LAR.

Due to the fact that these new reporting requirements became effective so recently, it is too early to draw any valid conclusions until we start receiving the new data next year. However, our examiners will consider information reflected on the register form as we conduct examinations this year.

Consumer Compliance Task Force Issues

As mentioned in our October testimony, the FFIEC Consumer Compliance Task Force is considering further possible actions for strengthening compliance with the fair lending laws. We addressed the establishment of mortgage review boards and the use of testers in our December response to the follow-up questions to our October testimony. Since then, the Task Force has attempted to identify mortgage review boards throughout the country. Very few active programs have been found. Representatives for the banking agencies conducted interviews in connection with the review boards in Boston and Detroit, as well as a mortgage partnership in Philadelphia. The Task Force is currently evaluating this information, and no further recommendation to the FFIEC has yet been made. The Task Force also is gathering more information about the inactive programs it found to understand why they are not active and to identify potential problems. We will continue to pursue this matter.

With regard to testing, the FFIEC on November 17, 1989 discussed a proposal from its Consumer Compliance Task Force to consider conducting a Fair Lending Audit, which would include testing at the pre-application stage. The consensus was to not pursue such an effort. The FDIC continues to support that position. We believe that it would be counterproductive for the financial institution regulatory agencies to engage in testing of depository institutions because of the adversarial relationship that testing would engender. The examination and supervision process depends not only on the training and ability of the examiner, but on the willingness of the institution being examined to be open and honest about problems at the institution. If the agencies were to engage in testing, we believe it would create a climate of mistrust that may jeopardize the examination process. Further, it is our view that testing at the loan application processing stage is unnecessary since the FDIC's fair housing examination procedures, as well as our complaint investigation procedures, already require examiners to review a sample of approved and denied home loans. FDIC examiners determine whether the information available in the records supports the reasons for denial stated in the adverse action notices and is consistent with the institution's mortgage lending policies.

The Task Force is also reviewing a proposed questionnaire format that could be used for the broad-based sharing of community contact information among the agencies. The questionnaire is being designed for use by Regional and field personnel. Final FFIEC action on this endeavor is expected in the next few months.

Compliance

The FDIC continues to share the concerns of Congress and the public regarding reports which indicate possible discrimination in mortgage lending. We remain committed to doing whatever is necessary to address these concerns. Institutions under our jurisdiction that do not comply with consumer protection and civil rights laws and regulations find that violations can result in increased regulatory oversight, administrative actions, and civil money penalties. An institution also is likely to be subject to CRA protests and complaints, which can result not only in denials of applications, but in costly time delays. However, the FDIC's overall experience, with few exceptions, has been that once a problem is brought to an institution's attention, steps are taken to correct it. No FDIC-supervised institution with a CRA rating of less than satisfactory has had an application approved without first agreeing to take appropriate corrective actions.

The following table indicates the CRA ratings for FDIC-supervised institutions examined during the past three years:

CRA RATINGS

Year:	1	2	3	4 and 5
1987	221	1,965	40	8
1988	307	2,683	58	12
1989	306	2,295	54	4

Our composite consumer compliance ratings are an additional measure of possible discriminatory patterns and practices. The following table indicates the composite compliance ratings for FDIC-supervised institutions examined during the past three years:

COMPOSITE COMPLIANCE RATINGS

Year	1	2	3	4 and 5
1987	319	1,617	290	16
1988	472	2,166	394	34
1989	449	1,885	298	28

Based on CRA and composite compliance ratings, it can be seen that the great majority of FDIC-supervised institutions continue to be in satisfactory or better compliance with the fair lending laws.

CRA protests by the public against applications provide the FDIC with an additional vehicle through which we can monitor possible illegal mortgage lending discrimination. The FDIC received ten CRA-related application protests in 1987 (against eight institutions); six in 1988 (against five institutions); and seven in 1989 (against six institutions). Of those submitted in 1989, six protests were withdrawn after the institutions made commitments to address the protestants' concerns, and one of the applications was withdrawn so the applicant could address CRA concerns raised during our investigation. Two protests (against two institutions) have been submitted during 1990. These are currently under investigation.

The FDIC's toll-free "hotline" is another useful indicator of possible lending discrimination practices. During 1989, the FDIC's Office of Consumer Affairs and our Regional Offices reported approximately 48,100 telephone calls for information and assistance. Of this number, 549 calls involved community reinvestment matters and 1,707 involved fair housing. For the first three months of 1990, nearly 17,030 telephone calls were reported, with 379 relating to community reinvestment and 372 concerning fair housing matters. Many of these calls were from bankers in connection with regulation revisions. In 1989, OCA and the Regional Offices also received about 4,400 written complaints and inquiries, 3 of which involved CRA issues and 4 of which involved fair housing. During the first three months of 1990, over 1,200 written complaints and inquiries were received. One of these involved community reinvestment and none involved fair housing. After investigating the inquiries, we found no actual evidence of mortgage lending discrimination in any of these instances.

Conclusion

In conclusion, we share the Subcommittee's concerns about mortgage discrimination, and we are committed to doing our part to ensure that financial institutions do not engage in this illegal practice. Over the past six months, we have made a number of significant changes in our consumer compliance program with the goal of improving its effectiveness. These changes include new efforts at community outreach, a new consumer compliance examination program separate from our safety and soundness program, and increased consumer protection training efforts. We believe that these changes will improve the FDIC's consumer compliance program.

ADDITIONAL QUESTIONS FOR FEDERAL REGULATORY AGENCIES

1. In how many instances over the past three years has your agency found substantive violations of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations? Provide some examples of how these substantive violations were resolved.

Thirty-eight substantive violations were cited for institutions examined from January 1, 1987 through December 31, 1989. Most were considered isolated violations and not a pattern of discrimination. In every case, we required management to make corrections, including amending their loan policies where necessary. When we forwarded examination reports to the institutions, they had to advise the FDIC of the corrective actions taken. Examiners are also required to follow-up on cited violations at subsequent examinations. Corrective actions were taken in almost all the cited cases and repeated violations generally were not found. (In those few instances where corrections were not made, we have increased supervisory actions to ensure that the institutions take corrective action as soon as possible.) By way of example, in one instance an institution had an illegal policy of automatically assigning young and elderly applicants a greater risk factor. This was one of many apparent violations in the institution. We required the institution to sign a Memorandum of Understanding specifying needed corrections. Also, the institution's policy was changed and other corrections made. Examiners verified the corrections at the next examination.

2. In how many instances over the past three years has your agency referred cases of possible discrimination to the Department of Justice for prosecution? What were the results?

No cases have been referred to the Department of Justice over the past three years. The FDIC has adequate authority to enforce compliance with the fair lending laws and regulations through increased regulatory oversight, administrative actions, and civil money penalties.

3. Has your agency found violations of the Fair Housing Act or ECOA (Regulation B) based on an "effects test" analysis? Can you provide any specific examples of how you have used this approach to prohibit lenders from maintaining loan policies which have a discriminatory effect on minorities?

Violations of the Fair Housing Act or ECOA are identified in the examination process through prescribed examination procedures. In following these procedures, our examiners review and analyze an institution's lending policies and procedures to determine if discriminatory practices are evident. Analysis includes an evaluation of whether any of the policies or procedures fail the "effects test." However, the FDIC does not separately track the individual methods, including the "effects test," that may be used by examiners to detect violations of the Fair Housing Act or ECOA.

4. How many fair lending written complaints did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation? Provide some examples of how these substantive violations were resolved.

From January 1, 1987 through May 1, 1990, we received 3,615 complaints related to the fair lending laws (ECOA, FHA, CRA, and HMDA.) None of them led to a finding of a substantive violation. The largest volume involved nationwide credit card operations, i.e., denial of credit applications. In one particular instance, the volume and nature of the complaints led to an examination of the institution based on our concerns about the allegations. While the examination did not reveal actual violations of the laws or regulations, the institution had failed to follow its own policies and procedures with regard to communicating its denials of credit to applicants, resulting in confusion on the part of applicants. We advised the institution to adhere strictly to its policies in the future and make any necessary corrections. The following is a breakdown of the written complaints by year:

1987	1988	1989	5/1/90
1,381	835	378	72

5. How many fair lending telephone calls did your agency receive over the past three years? Can you characterize these inquiries? Are there any patterns among these inquiries? What are complainants told in response?

Our Office of Consumer Affairs and eight Regional offices reported over 2,100 telephone calls related to the fair lending laws (ECOA, FHA, CRA, and HMDA) in 1987; nearly 3,100 in 1988; and about 5,600 in 1989. Many of the calls were from bankers concerning regulatory changes. Many of the other calls were from consumers with questions about credit denials or home ownership counselling requirements. We also received a number of calls from individuals involved in fair lending studies in their communities, and seeking general information. No patterns were noted nor was any particular institution the focus of the inquiries. Those wishing to register a specific complaint are generally requested to do so in writing. In every case, we investigate the complaints received and try to resolve the problem or provide necessary information.

6. Do appraisers, private mortgage insurers, or the secondary market play a role in discrimination? What should Congress do about the problem of under-appraisals of properties in minority areas? Would your agency detect this problem in its normal examination or complaint-response procedures?

Any group or individual involved in mortgage lending activities could play a role in mortgage lending discrimination, including financial institutions, appraisers, private mortgage insurers or the secondary market. We have no information, however, on which to express an opinion about whether appraisers, private mortgage insurers, or the secondary market actually play a role in such discrimination.

The FIRREA contains real estate appraisal reform amendments, the purpose of which is to require that real estate appraisals utilized in connection with federally-related transactions be performed according to uniform standards by individuals whose competency has been demonstrated and whose professional conduct is effectively supervised. Accordingly, the FFIEC established an appraisal subcommittee which early this year released guidelines for state certification and licensing of real estate appraisers. These new standards should help ensure uniformity and consistency throughout the appraisal industry.

With respect to under-appraisals, we have found no evidence of this practice through our normal examination process or complaint procedures. However, if we received any complaints or found any evidence of under-appraisals, we would investigate.

Senator DIXON. Thank you very much, Mr. Bovenzi.

And before I recognize Mr. Kluckman, may I say that I'm delighted to see here the ranking member, my good friend, the Senator from Missouri, Senator Bond. Do you have an opening statement, Senator?

OPENING STATEMENT OF SENATOR BOND

Senator BOND. Thank you, Mr. Chairman. I am very pleased that we are pursuing the issues discussed at the last fall's hearing on discrimination in home mortgage lending.

Please accept my apologies—and I address this to all witnesses—for arriving late and having to leave early; we are in the process of mark-up of the 1990 farm bill, which may be a long-going procedure that could, the way it's going today—may last through the summer, into the fall and the winter. [Laughter.]

But I have taken a brief break because I believe this is very important.

Bankers talk a lot about the regulatory burdens and I do think that we need to look carefully at whether imposing additional congressional mandates in banks is wise. Compliance with fair lending laws, however, should be the highest priority of both the banking—financial industry and the regulators. Fair access to credit is fundamental to insuring that everyone in our society has equal opportunities and I look forward to discussing with the witnesses how these goals can best be achieved.

We need to think carefully about which agencies would do the best job of seeing that the fair credit laws are obeyed. HUD certainly has expertise in the enforcement of the fair housing laws, while the bank regulators' primary mission is the safety and soundness of the banking system. I look forward to discussing with the witnesses how we can best and most efficiently insure the enforcement of the fair lending statutes.

Thank you, Mr. Chairman.

Senator DIXON. I thank my friend from Missouri.

Mr. Jerauld C. Kluckman, the Director of Compliance Programs, the Office of Thrift Supervision. Nice to see you, Mr. Kluckman.

STATEMENT OF JERAULD C. KLUCKMAN, DIRECTOR, COMPLIANCE PROGRAMS, OFFICE OF THRIFT SUPERVISION

Mr. KLUCKMAN. Chairman Dixon, Senator Bond, I am pleased to present the testimony of the Office of Thrift Supervision on measures we have undertaken in the past 6 months to strengthen our fair lending enforcement efforts. As we have testified in the past, our office is implementing a new program involving the use of specially trained compliance examiners who conduct separate examinations of savings associations for fair lending laws and other laws. In the past year, nearly a thousand specialized compliance examinations have been made. The program is scheduled for full implementation by the end of this year. The specialized compliance program serves as a centerpiece for fulfilling our fair lending enforcement responsibilities.

While the specialized program was started by our predecessor agency, the Federal Home Loan Bank Board, Director Ryan has asked me to assure the subcommittee of his commitment to this program.

Working with the banking agencies, we have devoted a great deal of effort since last August developing a new uniform rating system for CRA evaluations and a public disclosure procedure for these evaluations. We believe that we now have a mechanism in place to assure that examiners develop comprehensive, fair and reasoned CRA evaluations to benefit the financial institutions and the public.

Working through the Exam Council, we are also taking part in the exploration of four initiatives that would help strengthen enforcement of the fair lending laws:

First, the Task Force on Consumer Compliance is actively researching mortgage review boards.

Second, we have drafted an agreement on the sharing of information from community interviews.

Third, we will be considering the possibility of summarizing HMDA lending statistics and presenting them in the examination reports.

And finally, we will be looking into developing a media presentation on the subtle aspects of discrimination.

We have recently amended our nondiscrimination regulations to make them comport with the FIRREA changes to the Home Mortgage Disclosure Act. The new changes require financial institutions to maintain loan application registers much like those that savings associations have kept for the last 10 years. Although we have eliminated unnecessary duplication between the new HMDA register and the register required by our regulations, we continue to require all savings associations to maintain monitoring information not required by HMDA.

For example, savings associations are required to maintain data on the marital status and age of the applicants and various data regarding loan terms. This additional information facilitates the examiner's review for discrimination.

We have also been working with the Department of Justice in the fair lending area. We have agreed to share the results of our findings on one savings and loan association in Atlanta in which Justice representatives conducted part of their investigation while we were examining the institution. Justice is using a computer analysis to determine whether the institution's lending policies are being applied in a uniform manner to all applicants. We will study their analysis to determine whether it might be adaptable as a special examination tool.

Mr. Chairman, your invitation letter asked for our review of information relative to lending statistics from the recent past. Statistics available from our loan application register system for the first half of 1989 show that the rejection rate for both white and black mortgage loan applicants increased: 11 percent to 13 percent for whites and 23 to 29 percent for blacks.

While we do not have any specific explanation for the increases, one likely reason is that rising interest rates and advancing housing prices during this period would tend to disqualify more potential home buyers, particularly those with lower incomes.

We continue to use this data as part of our regular compliance examination process and to target certain geographic areas or institutions for special review. For example, we targeted 35 savings associations and 15 different MSA's for special nondiscrimination examinations. We selected savings associations in MSA's whose lending patterns showed a large difference in the rejection rate between white and black applicants. We have received nearly all the examination reports on these institutions and our preliminary findings do not indicate any systemic patterns of discrimination. However, we did uncover some practices, such as the use of high minimum loan amounts, that could serve to discourage applicants or have a discriminatory impact. Our district offices will assure that any necessary corrective remedies are taken.

Mr. Chairman, I want to assure you on behalf of the Office of Thrift Supervision, that we are committed to the vigorous enforcement of the fair lending laws and regulations. I believe that we have made positive inroads to attacking this problem head-on and have made significant enhancements to our approach. Moreover, we will continue to review and strengthen our fair lending enforcement efforts where appropriate.

I would be pleased to respond to any questions the subcommittee might have.

[The complete prepared statement of Jerauld Kluckman follows:]

Statement of

Jerauld C. Kluckman

Director, Compliance Programs

Office of Thrift Supervision, U.S. Department of the Treasury

Before the Subcommittee on Consumer and Regulatory Affairs

of the Senate Committee on Banking, Housing and Urban Affairs

May 16, 1990

Mr. Chairman and members of the Subcommittee, I thank you for your invitation to testify this morning on the progress the Office of Thrift Supervision has made in the past six months toward improving its examination and supervisory processes related to compliance matters, and more specifically, those associated with the fair lending laws and regulations.

During the past six months, we have continued to take affirmative steps to meet the agency's mission to "...ensure thrift compliance with federal laws and regulations, and to continue to provide a safe haven for savings, mortgage funding, and other services..." As indicated later in my testimony, we have continued with the planned implementation of our specialized compliance examination program. We are committed as a government agency to fulfill our responsibilities to the public and our mandate in this area.

Specialized Compliance Examination Program

As we testified before this Subcommittee twice in 1989, the OTS is proceeding toward full implementation of our program to use specially-trained examiners to conduct separate examinations of savings associations for compliance purposes. While this program was adopted in 1989 by the former Federal Home Loan Bank Board, I want to emphasize to the Subcommittee our commitment to maintain this specialized compliance examination program by our new Office of Thrift Supervision. Director Ryan has asked me to assure the Subcommittee of his commitment to the specialized compliance program as the heart of our efforts to enforce the fair lending laws and regulations.

The examinations under our new program, which began in April 1989, cover compliance with the full range of consumer protection and public interest laws and regulations, including those related to fair lending. During the past year, the OTS District offices have conducted just less than a thousand compliance examinations under the new program. We have a total of 129 examiners and analytical personnel in the districts assigned to the special compliance program and to handling consumer complaints.

Our specialized compliance examination program is scheduled to be fully implemented by the end of this year. Mr. Chairman, you expressed some concern at the Subcommittee's hearings on October 24, 1989, about our timeframe for implementation of this program. From an internal administrative standpoint, recognizing the realities of our own situation, we believe that our decision regarding the implementation period was reasonable. Given the number of issues faced by this agency as a result of FIRREA, full implementation by all of the District offices will take until the end of this year. We are pleased that some Districts will have their programs fully in place prior to this date. In order to assure that the agency, as a whole, meets the December 1990 deadline for full implementation, we will be working closely with any Districts needing assistance early this summer to identify precisely what remains to be done and to assist them in meeting the target date.

Compliance Training Programs

Since the October hearings, we have conducted three additional Compliance I Schools. These are two week programs for District staff selected to conduct compliance examinations. The curriculum includes 12 classroom hours on the fair lending laws and regulations and 12 classroom hours on the Community Reinvestment Act. We trained 60 staff at these three sessions of the school, bringing the total number trained to 92 since the first school was held in July 1989. Another session of the Level I school began this past Monday. This is a highly successful school and we have been fortunate to have had representatives from ACORN and the Center for Community Change make presentations at the school to give our examiners first hand the community point of view. Three more Compliance I Schools are scheduled for the remainder of 1990.

We have also developed a curriculum for a Compliance II School. That school will be one week long and be geared toward more experienced examiners. It will include two full days on Community Reinvestment Act and nondiscrimination matters. We anticipate holding the first Compliance II School during the third quarter 1990.

FFIEC Activities

We indicated to the Subcommittee in our October testimony and in a subsequent letter to you, Mr. Chairman, that we were working with the other agencies represented on the Federal Financial Institutions Examination Council (FFIEC) to explore various initiatives to enhance fair lending enforcement. The council gave approval to its Task Force on Consumer Compliance to investigate the feasibility of pursuing several different initiatives. These initiatives are:

- consideration of mortgage review boards;
- interagency sharing of information from community contact interviews;
- inclusion in examination reports of summarized Home Mortgage Disclosure Act data for senior management and the directors of an institution; and,
- media presentation (brochure, videotape, etc.) on subtle aspects of discrimination and potentially discriminatory practices.

The task force has just recently been able to turn its attention to mortgage review boards and the sharing of community contact information. As explained later in this testimony, the task force - and particularly agency staff with expertise in fair lending matters - has literally been consumed prior to and since the October 1989 hearings with the implementation of the FIRREA changes to the Community Reinvestment Act examination rating system and public disclosure of evaluations.

With regard to the consideration of mortgage review boards, which we are aware you may have a particular interest in, Mr. Chairman, the task force has gathered some preliminary information on the existence of such boards, their structure, and their operative practices. At this point, the task force will continue its research on mortgage review boards before reaching any conclusions about them.

The agencies have drafted an agreement with regard to the sharing of information gleaned from community contact interviews. We expect that we will all benefit from the sharing of this information. As you know, our staff, as well as those from other agencies, contact community representatives and the like during the examination process for the purpose of ascertaining the community's perception as to how well financial institutions are meeting credit needs, particularly those of low- and moderate-income neighborhoods in that community. Sharing this information will significantly enhance our knowledge of certain communities and create efficiencies by eliminating duplicative visits to the same community representatives by different teams of examiners from different agencies. In addition, the agreement will also include the sharing of information ascertained from any other agency CRA outreach efforts, such as any available specialized lending programs in a given community or public/private partnerships.

The idea of including summarized HMDA lending statistics in examination reports will be pursued once we can gain a better understanding of the best way to present such information in light of the changes to HMDA made by FIRREA. The media presentation concept on subtle aspects of discrimination will be addressed later this year.

CRA Rating System and Public Disclosure

Briefly stated, FIRREA amended the Community Reinvestment Act by requiring the agencies to use a new, uniform, four-tiered descriptive rating system and by making the results of CRA performance evaluations and the CRA ratings available to the public for examinations begun on or after July 1, 1990. In December 1989, the FFIEC published a notice requesting comment in the Federal Register detailing the new rating system and a disclosure format for making CRA performance evaluations public.

Comments received on the proposal were analyzed and a final version of the rating system and disclosure format was presented to the FFIEC for approval. At its meeting on April 20, 1990, the council approved the document and the OTS approved the package shortly thereafter. The final document was published in the Federal Register on May 1, 1990.

In addition, the agencies are in the process of promulgating changes to their CRA regulations that set forth the manner in which institutions will make their CRA performance evaluations available to the public. These regulations will require institutions to place the CRA performance evaluations in their CRA public files within 30 business days of receipt and make them available to the public upon request.

I cannot overstate the amount of effort that the agencies have put into this initiative. It has been extremely time-consuming and has required us to rethink not only the way we will meet the mandates of FIRREA in this regard, but our own operating practices as well. I believe that we have developed a workable product that will serve to provide the institutions and the public with fair, reasoned, evaluations on CRA performance.

Along with the development of these materials, the agencies also prepared a comprehensive CRA training program for examiners. During this month, roughly 700 staff members from the agencies will be trained in eight regional training sessions in four different cities. These are day and a half day sessions that are designed to explain the new rating system, disclosure format, and regulatory changes. Approximately 200 staff from OTS are attending these sessions.

The agencies are also planning the issuance of a pamphlet to explain to the public, community groups, and financial institutions the CRA-related changes contained in FIRREA.

Home Mortgage Disclosure Act Amendments

In connection with the amendments to the Home Mortgage Disclosure Act that were enacted as part of FIRREA, and the Federal Reserve Board's ensuing changes to its Regulation C which implements the HMDA, the OTS amended its nondiscrimination regulations to bring them into conformance with HMDA and to eliminate duplicative reporting burdens on savings associations. Since 1980, the OTS has required savings associations to maintain Loan Application Registers and to submit periodic reports based on the registers to the agency for aggregation. The output reports based on the data are used to identify trends and lending patterns to aid the examination process under the fair lending laws. A substantial number of the items contained in our register are now required by Regulation C. Consequently, it simply did not make sense to require savings associations to maintain two nearly identical registers. Generally, savings associations can comply with the register requirement contained in our nondiscrimination regulations by maintaining the register now required by Regulation C.

However, in the interest of public policy and to assure that our examiners would be provided with sufficient data to work with, OTS decided to require savings associations to also maintain some additional data items not required by Regulation C that they had been collecting since 1980. In addition to the items required by Regulation C, savings associations must also collect the marital status and age of an applicant, check a box that indicates whether the property that is the subject of a mortgage loan is in the institution's CRA delineated community, and record various data about the loan itself, such as its interest rate and term. These additional data items will be available for the examiner to review during the on-site portion of an examination. Moreover, our nondiscrimination regulations require all savings associations to compile the register, not just those that are covered under HMDA.

Special Nondiscrimination Examinations

In connection with our ongoing review of mortgage lending statistics available from our Loan Application Register/Data Submission Report System, our District offices conducted special compliance examinations in certain institutions focusing on the fair lending and nondiscrimination laws and regulations. First, we selected a number of Metropolitan Statistical Areas whose aggregate data indicated to us that there were sizeable differences between the rejection rates for black and white mortgage loan applicants. Next, we identified institutions within those MSAs whose data manifested unusually large differences between rejection rates for black and white applicants. Our appropriate District offices were asked to conduct special nondiscrimination examinations in these savings associations. These examinations covered compliance with the Equal Credit Opportunity Act, Fair Housing Act, Home Mortgage Disclosure Act, and our agency regulations regarding nondiscrimination.

In total, 35 special nondiscrimination examinations were conducted in 15 different MSAs. The examiners used the credit investigation procedures in our Compliance Activities Handbook as the basis for these examinations. We have received copies of nearly all of the examination reports associated with these examinations. Based on our preliminary reading of the reports, it does not appear that any systemic patterns of prohibited discrimination were uncovered. Some examinations revealed a large number of technical reporting inaccuracies in the Loan Application Registers themselves, and substantive deficiencies in loan underwriting standards that may, in some instances, result in the unintended discriminatory treatment of protected classes. For example, a few of the reports cite the practice of using unrealistically high minimum mortgage loan amounts. As stated earlier, we are in the early stages of our review of these examination findings. Please be assured, however, that any illegal practices will be subjected to the full extent of our enforcement powers.

Cooperative Efforts with the Department of Justice

As the Subcommittee may know, the Department of Justice sent letters to approximately 64 Atlanta-area mortgage lenders last year, requesting a variety of information on lending standards, policies, and practices, as well as loan application register data, where available. The DOJ and OTS agreed to cooperate with each other and share the results of our respective findings on one institution in Atlanta. This cooperation took the form of DOJ representatives conducting part of their investigation at the same time that OTS examiners were in the institution performing a special nondiscrimination examination. In connection with that investigation, the Department of Justice is utilizing computer analysis to help determine whether the institution's lending policies are being applied in a uniform manner to all applicants. The input for the analysis requires the collection of roughly 80 pieces of data from a large number of approved and rejected mortgage loan applicants.

We believe that each agency has much to gain by this sort of cooperative venture and much to learn from each other. We will be interested in reviewing the results of DOJ's computer analysis when it is completed in the near future.

Statistical Data

As you requested, Mr. Chairman, we have analyzed our HMDA and Loan Application Register/Data Submission Report (LARS/DSR) information since our October testimony. Our findings are presented below.

LARS/DSR

Our latest statistics generated by the LAR/DSR system is for the first half of 1989. These statistics indicate that nationwide the rejection rates for both whites and blacks increased from the second half of 1988. The rejection rate for white applicants has increased from 11% to 13% while the rate for black applicants has increased from 23% to 29%.

We are concerned about these changes and intend to look into the statistics further to pinpoint any primary locations where the increase is more apparent and/or determine whether any particular institution's lending pattern contributed substantially to the increase in the black rejection rate. We will then determine where special targeted examinations need to be undertaken.

I do want to reemphasize to the Subcommittee the danger of drawing conclusions about potential discrimination from these statistics. The differences in rejection rates, in and of themselves, do not indicate that savings associations are discriminating on a prohibited basis, as the data system does not enable one to draw such a conclusion. The data does, however, raise questions that examiners must address as part of the examination process. The significance of the differences cannot be ignored, but can only be explored and explained through vigorous field examinations that thoroughly analyze a given savings association's policies, procedures, lending programs, and criteria. The data does not provide any information as to an applicant's creditworthiness nor does it offer any information about a particular lender's credit or underwriting criteria.

Statistics showing a disproportionate number of loan denials from minorities, women, or other protected classes, or a disproportionate rejection rate in minority areas, raise questions which savings associations should be called upon to answer or which should be analyzed by examiners in their review of loan application registers in the examination process. While firm conclusions normally cannot be drawn from the DSR data, questionable flows and patterns are identified and explored as part of the examination process.

We are deeply concerned about any meaningful disparities that point to potential differences in the way members of protected classes are treated as compared to others in the lending process. While our data, and our analysis of it, does not manifest proof of credit discrimination, our new examination program is designed to make full use of available data and make certain that such matters are thoroughly addressed. I want to assure the Subcommittee that we are committed to investigating alleged instances of discrimination and monitoring the activities of savings associations in this area, as we have done in the recent past.

Review of Recent HMDA Information

A review of aggregate Home Mortgage Disclosure Act (HMDA) data for home purchase loans between 1981 and 1988 indicates that savings associations have reported 7,626,974 such loans or 60.20 percent of the total reported by all HMDA-covered lenders. Attachment A contains a table illustrating the numbers of home purchase loans made by all reporting lenders, those made by thrifts, and the thrifts' percentage of the totals for the past 8 reporting years.

HMDA data for 1988 also shows that thrifts have been significant participants in low-income, minority areas. National aggregates for home purchase loans show that thrifts made:

- 66.59% of the home purchase loans in low income, minority census tracts with a minority population greater than 50%.
- 63.67% of the home purchase loans in low income, integrated census tracts with a minority population between 15 and 50%.
- 64.55% of the home purchase loans in low income, minority census tracts with a minority population greater than 80%.

Savings associations were also active players in the market for home purchase loans in middle and upper income, minority census tracts. National aggregates for home purchase loans show that thrifts made:

- 70.42% of the home purchase loans in middle income, minority census tracts with a minority population greater than 50%.
- 72.38% of the home purchase loans in middle income, integrated census tracts with a minority population between 15 and 50%.
- 57.11% of the home purchase loans in middle income, minority census tracts with a minority population greater than 80%.
- 72.74% of the home purchase loans in upper income, minority census tracts with a minority population greater than 50%.
- 63.43% of the home purchase loans in upper income, minority census tracts with a minority population greater than 80%.

Questions Posed by the Subcommittee

In your letter of invitation, you asked that we respond to six questions. The questions and our responses follow.

1. **In how many instances over the past three years has your agency found substantive violations of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations?**

The OTS considers substantive violations to include those constituting evidence of overt discrimination, differential treatment of loan applicants on a prohibited basis, making significant errors with respect to maintaining a loan application register, not using the equal housing lender logotype in advertisements, or failing to furnish adverse action notifications. Over the past three years (1987 - 1989), 11.33 percent of the savings associations examined by the OTS have been cited for at least one violation of the Equal Credit Opportunity Act. In most instances, violations involve technical matters; examiners have cited 12 savings associations for substantive violations of the law.

Incidentally, we are in the process of developing a data base of examination statistics and cited violations to help us more accurately monitor the extent of compliance by savings associations.

Examples of how these substantive violations were resolved:

Our Districts indicate that violations are typically resolved through meetings with management without the need for formal agreements. Supervisory corrective action frequently involves the revision of underwriting guidelines by the institution, resulting in changes to policies and procedures, or the elimination of violative practices. Management often establishes committees or other such control points to review documentation of monitoring information and in some instances, implemented computer tracking systems for lending data.

An institution in the Des Moines District was found to have a poor record of helping to meet the needs of its delineated community due to an owner who was generally opposed to lending (according to senior management). This institution was placed under a supervisory agreement called a CRA Accord.

An institution in the Boston District was found to have committed substantive violations involving the incorrect compilation of LARS/DSR information. The violations resulted from a failure to collect monitoring information. That problem was addressed through a provision in a Cease and Desist Order against the institution.

2. **In how many instances over the past three years has your agency referred cases of possible discrimination to the Department of Justice for prosecution? What were the results?**

We have not found the need to make referrals to the Department of Justice over the past three years because we have been able to obtain compliance using our own supervisory powers. As I indicated earlier, we are working cooperatively with Justice in one of our examinations.

3. **Has your agency found violations of the Fair Housing Act or ECOA (Regulation B) based on an "effects test" analysis? Can you provide specific examples of how you have used this approach to prohibit lenders from maintaining loan policies which have a discriminatory effect on minorities?**

While we have found no cases where an actual "effects test" determination was made, the New York, Pittsburgh, Cincinnati, Indianapolis, Des Moines, Topeka, and San Francisco districts have found policies and procedures which could, in certain circumstances, have "effects test" implications. For example, the following types of activities have been noted occasionally by our examiners:

Minimum loan amounts.

Limited number of branches accepting applications.

Higher charges on smaller loans.

Loan denials based on age or location of property, (a violation of OTS regulation 12 CFR 528.2(a)).

Discounting appraisals (for factors already used to determine value - double counting). Example: lump sum amount deducted from appraised value for functional obsolescence when already factored into appraisal.

High downpayment/closing cost requirements or unrealistically conservative debt/income ratios.

Typically, situations are resolved through interaction with senior management without the need for formal enforcement action. The institutions are directed to remove any violative practices or policies immediately. When an institution contends that a particular policy or practice results from a genuine business need, the institution is requested by the examiner to evaluate the potential negative impact. They are required to either find some alternative means of achieving their aim or to take affirmative steps to counter the potential negative impact.

4. How many fair lending written complaints did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation. Provide some examples of how these substantive violations were resolved.

During the the past three years (1987-1989), consumer complaints alleging discrimination have represented approximately two percent of all written complaints received by this agency. A total of 691 such complaints were received and resolved during the three-year period, with the annual totals declining somewhat from 312 in 1987 to 198 in 1989.

Violations of the Equal Credit Opportunity Act or Fair Housing Act were found in 24 of these 691 complaints. For 13 of the 24 complaints involving violations, the lender made a voluntary adjustment after reviewing the case. In the remaining 11 complaints, adjustments were made in response to a supervisory request. (Complaint data, unlike examination data, does not distinguish between technical and substantive violations. We have assumed that any violation that required an adjustment, monetary or non-monetary, was a substantive violation.)

In one case handled in 1989, a complainant alleged discrimination on the basis of sex. The district office review revealed that the institution considered the lack of a telephone listing in the complainant's name in reaching a credit determination, in violation of Regulation B. The institution was asked to offer the complainant an opportunity to reapply and to refund any fees associated with obtaining credit elsewhere. The institution was also asked to conduct a file search to determine if other applicants were affected, in order to notify those applicants and offer to reconsider their applications. The institution has taken the steps requested, and the file search is currently in progress.

Fees were also refunded, in accordance with a supervisory request, by an institution that had denied an applicant's loan on the basis of previous exercise of his rights under the Consumer Credit Protection Act. Since the documentation supported the denial, as a sound underwriting decision, based on valid financial criteria, further remedies were not required.

5. **How many fair lending telephone calls did your agency receive over the past three years? Can you characterize these inquiries? Are there any patterns among these inquiries? What are complainants told in response?**

We would classify fair lending telephone calls as those raising questions about sex discrimination, racial discrimination, age discrimination, redlining, and disagreements regarding the reasons for loan denial. Not all of our District offices have maintained records of the types of telephone inquiries over the past three years. We can make a rough estimate that 4,000 fair lending calls were received. Of these, less than 20 complaints resulted in actual violations. There do not appear to be any discernible patterns among these inquiries.

6. **Do appraisers, private mortgage insurers, or the secondary market play a role in discrimination? What should Congress do about the problem of under-appraisals of properties in minority areas? Would your agency detect this problem in its normal examination of complaint-response procedures?**

As we indicated in our Report to Congress on Loan Discrimination (October 1989), we believe that there are other players in the field that may be contributing to possible discrimination against potential home purchasers. We recommended that other parties such as real estate agents, brokers, appraisers, and private mortgage insurers could be subject to strengthened enforcement activities. It may be appropriate for Congress to initiate hearings on this subject.

Our District offices generally indicate that under-appraisals would be detected through examination procedures regarding the review of loan denials, evaluation of the geographic distribution of loans, review of LARS/DSR information, and the review of residential appraisals during the examination of the residential lending process. In addition, this problem would be detected through the investigation and resolution of consumer complaints. The new appraisal standards being developed by the FFIEC and mandated by FIRREA should prove beneficial in this area. We suggest that Congress may want to delay pursuing any further action in this area until the new standards have been tested.

Attachment A

NUMBERS OF HOME PURCHASE LOANS
REPORTED UNDER THE
HOME MORTGAGE DISCLOSURE ACT
1981 - 1988

YEAR	ALL REPORTERS	THRIFTS	THRIFT PCT.
1981	729,374	386,489	52.99
1982	625,496	364,908	58.34
1983	1,154,709	754,861	65.37
1984	1,255,166	822,965	65.57
1985	1,371,892	816,443	59.51
1986	2,233,257	1,337,407	59.89
1987	2,664,757	1,613,763	60.56
1988	2,635,408	1,530,138	58.06
TOTAL	12,670,059	7,626,974	60.20

REJECTION RATES BETWEEN BLACKS AND WHITES

Senator DIXON. Well let's just start with you, Mr. Kluckman, because you skipped over a statistic that I find, in the first instance, appalling and, in its increased numbers, shocking:

You mentioned that from the second half of 1988 to the first half of last year the rejection rate for white applicants increased from 11 to 13 percent, while the rate for black applicants increased from 23 to 29 percent. In other words, prior to the second half of 1988, whites were rejected 11 percent of the time but blacks were rejected twice as much, 23 percent of the time.

The new numbers are, since the second half of 1988 and up until now, whites are rejected 13 percent of the time but Blacks are rejected 29 percent of the time. So instead of being rejected two-to-one, they're now being rejected, whatever the math is, a little worse than that.

What's the message in this? I want to first comment before I pursue the question: I think I would be compelled to state that I'm pleased with some of the responses that I'm getting from all of you. I see this increased effort to get at the truth of this, but I mean the raw data still says to me as chairman of this subcommittee something is the matter out there.

What do you say about those numbers?

Mr. KLUCKMAN. We are concerned about the numbers, as we had been in the past when they were 23 percent, as well as we are when they are 29 percent.

Senator DIXON. Yes.

Mr. KLUCKMAN. I'm fearful, though, that people make conclusions that this evidences discrimination. And there are a lot of things that go into these numbers that do not permit one to draw that conclusion.

For example, the basic numbers themselves do not reflect any information about the creditworthiness of the applicants. In other words, the fact that an applicant is rejected shows as a rejected statistic but we have no information as to the creditworthiness——

Senator DIXON. Well if I may interrupt at that point: are we trying to find that now?

I hear all of you saying what you're doing to get more raw data. And we continue to pass in every vehicle that comes along here—my friend from Missouri, I'm sure, would agree—more and more legislation directing you to find out more and more things.

Will we some time have an analysis of this? I mean, can you some time say to this Senator, Mr. Kluckman, or this committee: Look, don't be worried about that, there are a lot of good reasons inside these numbers that compel us to draw a conclusion that no discrimination is taking place here, notwithstanding the outrageous disparity in these numbers?

Mr. KLUCKMAN. Well I think that's exactly what we try to do in our examinations. We use these numbers and we use the loan application registers when we're making the examinations to try to determine on an individual basis whether a particular applicant has been rejected for discriminatory purposes or whether the applicant does not meet the underwriting criteria, whether the white applicant who has equivalent characteristics to a black applicant are both rejected or both approved, we try to look at that in the examination process and——

Senator DIXON. And don't we have some of that raw data now that one could bring to a further hearing? For instance—I'm an old trial lawyer and I like to look at the facts: Do we have situations where a black man or woman with a house that was adequate in value, made an application that was rejected that can be compared against a loan to a white man or woman in similar circumstances with similar value in the house for a similar loan of a relatively comparable amount? Are we doing some of that apples-against-apples and oranges-against-oranges sort of thing?

Mr. KLUCKMAN. Absolutely we are. We are looking at that as part of the examination process.

Senator DIXON. And have we gotten to the point yet where we can draw any conclusions from it?

Mr. KLUCKMAN. Our preliminary indication is based upon, the 35 special exams we've done, that we are not finding smoking guns, we are not finding instances where blacks have been rejected for discriminatory reasons——

Senator DIXON. Well then I ask you: Why are they rejected twice as much?

Mr. KLUCKMAN. Again, I go back to the point that the issue of creditworthiness, the issue of income all have implications in this.

Senator DIXON. Yeah, but I'm talking about a black man and a white man with similar income and similar valued homes, an apple against an apple, making an application for the same kind of a $10,000 loan. Now they're two equally creditworthy people, presumably——

Mr. KLUCKMAN. They're not necessarily two creditworthy people——

Senator DIXON. That's why I want it further developed.

Mr. KLUCKMAN. They may have similar characteristics but they may have different credit ratings, for example.

Senator DIXON. One pays more slowly than the other?

Mr. KLUCKMAN. That may be, yes.

Senator DIXON. Has more debt?

Mr. KLUCKMAN. That's very true.

Senator DIXON. Well do we find that?

Mr. KLUCKMAN. Yes.

When our examiners examined these particular instances why loan applications have been rejected, there are economic reasons, there are reasons for failure to meet the underwriting standards of the institutions, that impact upon this.

Senator DIXON. Well now let me interrupt to say this:

At the last hearing, you folks—incidentally, I'm not just picking on you, Mr. Kluckman, because I think all of you are doing better. I'm just trying to get at the facts. That's what we're supposed to do; I hope you understand. This isn't a matter of being, you know, here to tear at you, it's to try to find the truth.

At the last hearing you folks reported a simple 2-to-1 ratio between black and white rejections. The Atlanta Constitution published an analysis showing that in their city and in most cities in America high-income blacks were rejected more frequently than low-income whites.

Is that what you're finding?

Mr. KLUCKMAN. That's what the statistics show, that's correct, in that particular instance. We have no quarrel with that statistic; we believe that's accurate.

Let me point out too, Senator, that we are the only agency that has this kind of information.

Senator DIXON. I realize that. I want to say to you, sir, that at the last hearing the developments that we saw were to the effect—and again I say I'm not picking on you—that your agency had probably done the most at that time to develop this information.

But I pursue it assiduously because this Senator, at the final analysis of it, does not yet see persuasive evidence that discrimination is not taking place.

Have you turned any case over to Justice?

Mr. KLUCKMAN. No, we haven't.

Senator DIXON. How many cases do you have?

Mr. KLUCKMAN. Cases of what, Senator?

Senator DIXON. Well you say a thousand exams have been made; you've testified.

Mr. KLUCKMAN. That's correct.

Senator DIXON. Well how many did you think looked a little bit questionable out of a thousand?

Mr. KLUCKMAN. Well I don't have specific details on that.

Senator DIXON. You don't know how many looked questionable out of a thousand?

Mr. KLUCKMAN. Questionable in terms of discrimination?

Senator DIXON. Yeah.

Mr. KLUCKMAN. Well let me say that we are finding some instances where applicants may not have been given the full opportunity to provide a written application; we're concerned about that. We are finding instances where there are some underwriting standards that may have the impact of discouraging applications from protected classes, for example, high——

Senator DIXON. Mr. Kluckman, do you know that staff tells me that there isn't a single regulatory agency that has turned one case over to Justice and that the penalty for failure to get a loan where there's what we think decent evidence of racial discrimination is you get a chance to make another application.

I mean, would you correct me if I'm in error?

Mr. KLUCKMAN. I don't think that's the penalty, making another application. If we do find discrimination, we make sure the institution has instituted procedures to stop it, stop future violations, and we would make them correct the violations that have taken place by perhaps offering the applicant the opportunity to prepare another application or to change any term—if higher interest rates were charged on that particular applicant, to make adjustments in the loan at that time.

Senator DIXON. Well I thank you, Mr. Kluckman, I'm going to move around the table a little bit.

But I do want to observe for all of you that, you know, it's a miracle, it continues to be a miracle that the numbers are so bad and we never find anybody in this whole country that has done anything so gross that they ought not to be penalized on at least one occasion to send a message to the whole country: Look, a person should get more than a slapped wrist around here in continuing what I continue to suggest is an egregious practice.

I mean, I don't care the color of a man, if that man has the collateral—or woman, as the case may be, I'd better hurry to say—ought to get the loan.

It's your day in court, Mr. Bond.

Senator **BOND**. Well thank you, Mr. Chairman. I have to say I share your concern. While the simple statistic, 29 percent rejection for blacks versus 13 percent rejection for whites may not prove discrimination, it certainly gives one real pause to figure out why on a broad basis there's such discrepancy.

I might ask that other regulators as to whether—you've been talking about thrifts. Mr. Bovenzi, do you see figures like that in your work? What do you see in the banks?

Mr. **BOVENZI**. Senator, I'd like to say that I share your concern. I would not want to jump to the conclusion that the increased rejections between blacks and whites could be solely due to income or factors that can be explained away. I'm not ready to dismiss the idea that there's discrimination.

We're trying to look at this in every institution we go into, as are the other regulators, and we are trying to get as detailed data as we can to get the answers to all of these questions. And, as you know, we are finding some substantive violations: In the past few years, we've found 38 substantive violations against anti-discrimination——

Senator **BOND**. What did you do with those, were those referred to Department of Justice?

REFERRALS TO THE DEPARTMENT OF JUSTICE

Mr. **BOVENZI**. They were not referred to Department of Justice. We take a stepped approach in trying to get the institution to correct its actions on its own. If they don't—we would move toward civil money penalties. But in all cases when we point things out to the institution they take steps to correct them. Sometimes that means removing someone from a job.

But we have not reached a point where we have referred things to Justice; they've always taken steps when——

Senator **BOND**. But even when you find discrimination they get, as the chairman suggested, they get a free bite at the apple: Just don't do it again and nothing will happen to you.

Is that enough to change behavior? Do you think that's—to say keep doing what you've been doing until we catch you one time and then you'll have an opportunity to change it, is that sufficient incentive to get changes?

And I would assume that the vast majority would want to comply but where you find a small group who do not——

Mr. **BOVENZI**. It has in our experience proven to be effective to this point. We have not gone back to find patterns of practice or institutions that continually act the same way. When something's pointed out they take steps to correct them.

Senator **BOND**. Do you have figures similar to Mr. Kluckman on the percentage rejection rate?

Or maybe I ought to ask some of the—on banks, do you have similar rejection rates?

Mr. **Bovenzi**. I don't have those figures.

Senator **Bond**. Mr. Herrmann, would you have or——

Mr. **Herrmann**. Senator **Bond**, I share the view of Mr. Bovenzi. The statistics are disturbing to us as well. And creditworthiness really remains a key issue. But in the instance that Chairman Dixon describes where we have a parallel circumstance; Credit, income, et cetera, that clearly reflects discrimination.

I would suggest to the panel that insofar as the remedies, they may be less than you would presume in the ordinary case: The reimbursement of fees—I think just going back and trying to put things back where they were is very difficult in the case of mortgage lending discrimination, because something has happened in the interim. The expense to the institution in this case is really significant.

I'd also like to mention for the chairman and Senator Bond that we are currently consulting with Justice on one case; we are in the midst of working with them on a referral on a bank in our western district.

Senator **Bond**. But do you have figures on the overall percentages such as Mr. Kluckman gave, the 29 versus 13?

Mr. **Herrmann**. No——

Senator **Bond**. Those groups were not available?

Mr. **Herrmann**. No, sir, I really don't have numbers on that.

Senator **Bond**. All right.

USE OF TESTERS FOR FAIR LENDING

I might ask Mr. Mansfield: HUD has used testers for fair housing enforcement in rentals and sales. Have you or do you contemplate using testers for fair lending and at what stage could those testers be utilized?

Mr. **Mansfield**. I do contemplate using testers for fair lending. The answer, the simple answer would be next year, fiscal year 1991. That may require some explanation.

Senator **Bond**. I would be interested to hear how you propose to proceed.

Mr. **Mansfield**. The area we'd be looking at that would be in the title 8 area and, as I mentioned, I'm looking at this as a 3-year process. Secretary Kemp has instructed me to set up a program and part of that is building a strong foundation. So we're in the process of getting a case processing and management system up and running. And we have accomplished the goals to date so far.

And in the area of fair lending, in my management plan for this year we are projected to move into that area on the Secretary-initiated investigations and complaints during the fourth quarter to develop the ways of doing and start doing it and move into it next year. So——

Senator **Dixon**. Would my friend from Missouri be offended if I piggy-backed on this?

Senator **Bond**. Please.

Senator **Dixon**. I thank him for bringing up the question of testers. I just want to be open and above board about this, Mr. Mansfield, since we've gotten into testers and I think—and my friend Mr. LaWare had mentioned their contemplated thoughts about that as well, if my notes serve me.

I'm told there is a problem here, unlike testers in the purchase of a home, when creditworthiness is investigated and you get the credit report and other things, the use of the same tester over time requires frankly, if you'll forgive the expression, some cover.

I'm wondering are you concerned about how you would do that or are you giving that some thought? Forgive me for——

Mr. **Mansfield**. Yes, sir, we are looking at the area——

Senator **Dixon** [continuing]. Jumping in on that, but it's a matter I'm concerned about.

Mr. **Mansfield**. There's more problems than that involved in this because what we think is that a large part of the problem is going to be in the preapplication phase where people may not get to put pen to paper, which would be the evidence to take them forward. So we're looking at the preapplication stage as how do we handle that.

And then the other problem is—refers to some answers and questions asked before is if we're in the testing area it's going to be hard to set up a case history where we've got equivalency: In other words, credit histories and, you know, amounts of income and payment rates and those things.

So it's going to be a little bit more difficult, I think, to establish what the equivalency of the testers is in this area. But we are looking at it and we're looking at using that and working with the fair housing groups to move forward in this area.

Senator **Dixon**. Thank you. I didn't mean to jump in.

Senator **Bond**. That's all right.

I'm sorry I missed your testimony originally, Mr. LaWare, but according to our chairman you have suggested possibly using testers.

What are the—are testers more efficient than just using statistical information? Do you have problems with the statistical information, the broad statistics that we've discussed earlier?

Mr. **LaWare**. Senator, up until now the Federal Reserve has not had available to it the applicant information. Under the new HMDA reporting system which are developing and which will go into effect later this year, applicants can be tracked and we will be able to do something about tracking the disposition of applications and get a lot more reliable information there.

At the moment, we have authorized the use of testers to the examiners in our Federal Reserve Banks who do the examinations. What they are instructed to do is if, for example in discussions with community groups, the suggestion is made that applicants are being discouraged on a discriminatory basis from even filing an application and if, on investigation, there seems to be some truth in that, some reason to believe that that's going on, then our examiners would be authorized to use a testing mechanism at that stage.

To go beyond that, you have to, as the chairman said, create cover. It's expensive, it's difficult to do and one case doesn't prove very much; you have to do it on a big enough sample to make the case. So we have not used that. And I believe that we have probably not used the tester system on the prescreening basis because, on investigation of the very few instances where it has been suggested that discriminatory discouragement was going on, we haven't been able to verify that it smelled bad enough to go after it.

Senator Bond. I'd just—I'd like to, if the chairman will permit me, like to ask one general question——

Senator Dixon. Please do.

BORROWERS SHOULD KNOW THEIR RIGHTS

Senator Bond. interventional radiologicalMost of you said that you've had very few reports of lending discrimination, few consumer complaints. Is there something that ought to be done so that potential borrowers would know more about their rights and know how to go about filing complaints? Is part of the problem that consumers are unaware of their rights?

I'd open that to any of you to comment.

Mr. LaWare. Senator, I mentioned in my testimony that we have undertaken a communications program, both to alert borrowers to the credit granting process and what goes on there and to tell them what they need to know and what recourse is available to them. We have also invited some 700 community, civil rights, and governmental groups to cooperate with us in identifying consumers who feel that they have been discriminated against so that we can work with them in trying to root those practices out.

The real problem is to find out on a precise enough basis where the red flags are within an institution, in order to go after problems and try to get a remedy.

Senator Bond. Mr. Herrmann.

Mr. Herrmann. Yes. Senator Bond, I'd like to add to Governor LaWare's comment on that. That is one of the initiatives of the Council and we think there is some value in that. I think the key, as always, is to make this information, this customer information understandable and not legalistic. And as Governor LaWare suggests, we would like to enlist representatives of bank customer groups to help us with that information. I think that really would be a key to making it the kind of worthwhile information that would legitimize a complaint.

Senator Bond. Any other comments on that?

Mr. Mansfield.

Mr. Mansfield. Yes, sir. I think you're right. And we have two programs, the FHAP [Fair Housing Assistance Program] program and the FHIP [Fair Housing Initiatives Program] program run out of HUD Fair Housing. Both of those——

Senator Dixon. FHAP and FHIP.

Mr. Mansfield [continuing]. Have education and outreach components of it and working with state and local human rights agencies and with the fair housing groups. We would like to see more information gotten out.

Senator Bond. Thank you very much, Mr. Chairman.

Senator Dixon. Well I thank my friend from Missouri. I think I'll again piggy-back on his question about whether sufficient information is being given to the consumer, the loan applicant. I think that's a point well made and one I had hoped to develop here, and I thank my friend from Missouri for his usual incisive questioning about that.

Let me follow right after that with this question:

COPY OF APPRAISAL FOR APPLICANTS

It is suggested that to have a copy of the appraisal made available would be useful to those applicants who are denied their application for a loan, particularly in those cases where there would be suspicion of discrimination in the process. And I would invite the observation of each of you about that.

Mr. LaWare.

Mr. **LaWare**. Well I see no reason why the applicant should not have a copy, particularly if the applicant has paid for the appraisal——

Senator **Dixon**. And I wanted to hurry to indicate to you that in anything we crafted—and we'll have a vehicle shortly in this subcommittee that I'm satisfied the committee will mark up—we'd see to it that it was clear that there was compensation to the financial institution for the appraisal either in the form of the cost of the appraisal itself or otherwise. But you don't see any problem with making available to the applicant the appraisal——

Mr. **LaWare**. Certainly not.

Senator **Dixon** [continuing]. Upon which the refusal is predicated?

Mr. Mansfield.

Mr. **Mansfield**. I don't see any problem at all, sir.

Senator **Dixon**. Mr. Herrmann.

Mr. **Herrmann**. I don't see any problem with that, sir.

Senator **Dixon**. Mr. Bovenzi.

Mr. **Bovenzi**. I don't either.

Senator **Dixon**. Mr. Kluckman.

Mr. **Kluckman**. No problem. And I understand that's practice typically——

Senator **Dixon**. I regret to say it is not our understanding.

It is not, as I'm told, Mr. Kluckman—I don't mean to argue with you about it—general practice.

Thank you.

Well to give you an example of that, if I may come back for a moment to a specific case brought to my attention here. [Displaying document.]

I hold in my hand an application made by a woman from Tulsa: Applied for a $10,000 second mortgage home improvement loan. She was turned down because the appraisal for the house was only $10,000. The appraisal reviewed no comparables. The appraiser did not enter the house. The justification given was that her house needed exterior painting and several surrounding houses were poorly kept. The woman claimed the house was worth $55,000. Subsequently, the woman was offered a car loan of $10,000 at a higher interest rate.

The OCC did not in any way investigate, may I say, Mr. Herrmann, whether the appraisal reflected market value or prejudice against a low-income minority neighborhood. Also I'm informed

OCC did not look at whether that bank made any loans in that neighborhood or comparable neighborhoods.

It's considered a common example of discrimination, which one of the Detroit witnesses testified about at our last hearing, when a minority applicant is offered a loan but on less favorable loan terms than the ones for which she applied.

Now this, to me, is the kind of thing—I've read this whole report on this. This is what in the old days we used to call a windshield appraisal. Drove by. Because of the factors—"Per your request I did a drive by of the abovementioned property. House is in a deteriorated state; in need of repair. Neighborhood has a number of vacant houses. Those homes could be purchased very reasonably"—the guy's guesswork, I guess.

"Because of these factors we would place a value at no more than $10,000."

We've got a picture of the house here.

I mean, don't we need to look into more when we look at these things than apparently was done there?

Mr. HERRMANN. To respond, Senator Dixon——

Senator DIXON. And I'm not picking on you; every agency I could find examples——

Mr. HERRMANN. No, no. I appreciate it.

We provided that transaction to staff to really get across the point of the difficulty of compliance.

Senator DIXON. I know you did. And when I looked at it, I didn't get the same impression you got.

Mr. HERRMANN. And I feel that is one——

Senator DIXON. I don't mean to be offensive when I say this, but I thought you could have done more at your agency.

Mr. HERRMANN. I understand, Chairman Dixon.

With 43,000 complaints over a 3-year period, unfortunately, there are situations I think where we miss the point.

Of course, you're aware that last year Congress passed a law relative to appraisals. My judgment is as that proceeds and the regulations are implemented surrounding it, this kind of a situation would not take place.

Senator DIXON. Well I just want to return to one more thing. And I realize we're early on in these attempts to analyze raw data.

You know, I have to say candidly I think all of you would get a better grade on my report card this year than you did last fall and obviously part of that is due to the fact that you have more information available, and I take that into account.

But I continue to look at all this raw data that is not adequately analyzed and, you know, like in Atlanta you've got five times the chance to be turned down for a loan if you're black than you do if you're white.

Is that a correct——

Excuse me. I am corrected by counsel.

In Atlanta, there are five times as many loans in white neighborhoods as in black neighborhoods.

In, I regret to say, the greatest city in the world, Chicago, 3½ to 1.

Now, you know, I hear what you're all saying. Mr. Herrmann, we started not because I was picking on you, you were just the last guy to testify. But these numbers have to be meaningful in some respect. Are we trying to analyze that to find out why that's so?

Mr. **LaWare**. Yes.

And it will help when we get the additional data so that we can track these applications——

We know how many loans are made and it's roughly five or six times as many in a comparable census tract for whites as it is for minorities——

Senator **Dixon**. In Atlanta, as an example?

Mr. **LaWare**. In Atlanta. In the particular data that you've been looking at, Mr. Chairman——

Senator **Dixon**. Yes.

Mr. **LaWare**. But we don't know how many applications there are. Existing HMDA data does not include the lending activities nonaffiliated mortgage lenders who are typically more active in minority neighborhoods—and I'm not even going to speculate as to why. That information will be in the new HMDA data. So we'll have a much more accurate way to track exactly what the patterns are.

Senator **Dixon**. Let me interrupt at that point:

When will the new HMDA be available to all of you? I should know that. I've been told it, but I forget.

Mr. **LaWare**. The process for collating it, collecting it, it is still in the process of design. The Exam Council is due to look at the final proposals, I believe, on the format for the design within the next few weeks.

Senator **Dixon**. Could you all have your aides help you, as I must from time to time, and give me a finite date?

Mr. **Herrmann**. I believe, Chairman Dixon, the reports are due in the first quarter of 1991. And information should be available by the last quarter.

Mr. **LaWare**. Well fall of 1991.

But it's a massive job to do this data collection. And that's what we're in the process of doing at the moment.

ADVICE FROM FAIR HOUSING AND CIVIL RIGHTS GROUPS

Senator **Dixon**. Mr. LaWare, you testified that you'd sent out 700 letters to fair housing and civil rights groups asking them for their advice and their suggestions and their leadership in determining a sensible process——

Mr. **LaWare**. And to help us——

Senator **Dixon** [continuing]. I congratulate you for that.

I take it that was fairly recently done?

Mr. **LaWare**. Yes.

We are asking them to help us identify individual consumers who believed that they may have been discriminated against and to refer them to us so that if we can look into their complaints.

Senator **Dixon**. Now I'm told that was very recent. What was the date that you sent out these letters?

Mr. **LaWare**. Excuse me.

About 2 weeks ago, sir.

Senator **Dixon**. Would you enlighten this chairman by suggesting when you would be able to make some kind of an analysis of that and further enlighten us on the views of these 700 fair housing and civil rights groups in the country?

Mr. LAWARE. Well we need to give it a reasonable amount of time——

Senator DIXON. Sure.

Mr. LAWARE [continuing]. Not only for a response from the groups but from individuals whom they may identify.

I would think we'd begin to be able to give you a pattern certainly by the end of the third quarter.

Senator DIXON. I see your people nodding yes behind you.

Mr. LAWARE. Well that's good. [Laughter.]

I hope I'm with them.

Senator DIXON. By the end of the third quarter.

Mr. LAWARE. Yes, sir.

Senator DIXON. So that toward—well now it being an election year we take into account at least that we may get out of here in October some time, but I may come back to you all toward the end of the session with a follow-up on this and we could hear from you about those responses——

Mr. LAWARE. Whatever we have, we'll share.

Senator DIXON. We could hear from Mr. Mansfield more about their thoughts about the testing process, how testers might be employed. That would be very helpful.

MORTGAGE REVIEW BOARD

What about the mortgage review board? You touched on it, Mr. LaWare, and others have suggested it in past testimony. How is that working?

Mr. LAWARE. We're looking at what kind of a mortgage review board makes the most sense. There are basically two patterns.

One in which a group of participating lenders look at applications by people who have been turned down and who believe they have been discriminated against. If it is found that the applicant is creditworthy, that loan will then be assigned to one of the participating lenders. I believe that's the pattern followed in Boston.

The Philadelphia pattern has a greater appeal. In this case, action is taken before a loan is turned down and before a complaint has been filed. In other words, the 11 leading mortgage lenders in Philadelphia have gotten together—and this goes back 13 or 14 years—gotten together and decided that where there was a possible turn-down, where there might be a threat of discrimination or of unfair credit practices the application is reviewed before it is turned down and, in most cases—well, about half of those cases—the loan is finally made; in about a third of those cases it is finally turned down by this panel where they agree that the underwriting standards were not met and, in other cases, it is referred to the institution where the application origination was made, perhaps for redoing the application.

Over a period of about 13 years, they have made about $180 million worth of loans to people who might otherwise not have obtained a loan. And that is an appealing practice.

We are certainly encouraged by the thought that that might be adopted in a lot of other cities. As you know, Boston and Detroit have been the models for the post-turn down pattern and Philadelphia has expanded its activity now to the entire Delaware River Valley because it has been as successful as it has. I think that is a pretty positive program.

Senator DIXON. Thank you, Mr. LaWare.

SPECIAL ASSISTANT FOR FAIR HOUSING

Mr. Herrmann, you refer in your testimony to the fact that you have a special assistant for fair lending. How has that program worked?

Mr. HERRMANN. That emanated back 10 years ago, Chairman Dixon, from a case then where a group of bank customers filed a complaint against all of the regulatory agencies and that was part of the voluntary settlement at that time. That gentleman formerly was with HUD and now works with us, advising us, helping us with the statistics, trying to give us counsel as to how to proceed in the right direction on this whole area.

Senator DIXON. Mr. Herrmann, I don't want to take advantage of you, are you aware of the fact that your special assistant for fair lending has resigned?

Mr. HERRMANN. No, I'm not.

Not as of last Friday.

Senator DIXON. I am compelled to advise you that I am informed that effective this morning your special assistant for fair lending has sent in his resignation effective this date. I have it in hand.

Mr. HERRMANN. I'm sorry, Senator Dixon, I arrived here at 9 this morning, and I was in the office at 7. I have no knowledge of that.

Senator DIXON. Your staff has none?

VOICE. We do not.

Mr. LAWARE. I'm just checking my staff, Senator. I wanted to make sure that——

Senator DIXON. Is Ronald E. Wienk your special assistant for fair lending?

Mr. HERRMANN. Yes, sir.

Senator DIXON. Well I have before me——

Mr. HERRMANN. I'm sorry, Senator, that has just been delivered to me. It came up from the back of the room.

Senator DIXON [continuing]. A memorandum to Robert L. Clarke, Comptroller of the Currency, from Ronald E. Wienk, special assistant for fair lending, Re: Resignation.

> Effective immediately, I resign as your special assistant for fair lending.
>
> I believe I have accomplished all that I can accomplish with regard to OCC policies to monitor and promote banks' compliance with laws—including fair lending laws.
>
> As the primary architect of the Compliance Program, I provided an efficient, effective means through which the OCC could fulfill its compliance regulation responsibilities. Unfortunately, ineffective—indeed, vacuous—management in Bank Supervision Policy has been the principal impediment to full realization of the regulatory benefits of the Compliance Program.
>
> Regarding overall compliance performance by national banks, suppression of the program's initial report of findings is a serious deficiency in OCC's regulatory performance— a disservice both to OCC examiners and to national banks.
>
> Regarding fair lending policy, the OCC actually has regressed over the 8 years since I accepted an offer to join the agency.

OCC's failure to adequately perform its compliance regulation responsibilities—particularly with regard to fair lending—prompts my resignation.

I regret having to resign. I entered Federal Government service 15 years ago and remain dedicated to improving public policy. I still believe that one of the most important roles of government agencies is to protect citizens—as consumers, depositors, credit applicants, and, generally, "just" as people. Unfortunately, too many individuals in OCC management positions do not seem to share that view.

I have concluded that I will have a greater, positive impact on policy—including OCC compliance supervision policy—from a position outside the agency.

Mr. HERRMANN. I'm sorry, Chairman Dixon, but I for the first time, read right along with you that same memorandum. So I think it's very difficult for me to react in any way except total surprise.

Senator DIXON. Well, may I say I don't know Mr. Wienk and he has not talked to me about this, but it continues to concern this Senator because, while I hear how much more everybody is doing, I sense the frustration among groups that come to see me that represent those people out there that say they're not being treated squarely so far as the loan policies in the financial institutions in our country are concerned. And I just want to say I'm going to be the skunk at the picnic.

I had a hearing last fall and I'm having one now and I'm going to have another this fall. I don't want to do anything to suggest without facts here, you know, that something is wrong out there, but you know I have to say gentlemen—not as a common scold, but just because the facts are there—that there's never been a case referred to Justice.

Who said they were going to send one, was it you, Mr. Herrmann?

Mr. HERRMANN. Yes, sir.

Senator DIXON. Well good, maybe that will help.

We ought to look at these testers. I think we ought to get the copies of the appraisals for people so that at least they can go to a lawyer and sue if they think that they've been abused in the process.

And I think that the mortgage review boards have to be used more and I think we have to find some way—you know, this is a great government, it's got a lot of people with good green visor caps around to analyze this raw data and find out why these facts keep on tormenting us.

Let me just get back to you a minute, Mr. Mansfield, again, not picking on you either, but you had 155 cases, I'm told, that you looked at. Is that right?

Mr. MANSFIELD. I believe the number was 342, sir, and the 155 number, I think, was the number of those——

Senator DIXON. Oh yeah, 342.

Mr. MANSFIELD [continuing]. That were administratively——

Senator DIXON. 155 closed. Does that mean you found nothing there?

Mr. MANSFIELD. It means that they did not perhaps meet the procedural requirements of the new law, for example, the time frames or that they weren't, you know, eligible under the time frames or other——

Senator DIXON. Couldn't make any kind of a case for 155 of the 342.

Mr. **Mansfield**. That means that we found insufficient evidence of discrimination to move foreward to conciliation.

Senator **Dixon**. Then you said 136 are not resolved. Does that mean there's 136 that may be cases?

Mr. **Mansfield**. Yes, sir.

Senator **Dixon**. And then you had 14 something. What was that? You went a little quick for me to make all the notes.

Mr. **Mansfield**. I believe the 14 is those that we have achieved a conciliation or settlement. And I——

Senator **Dixon**. You worked them out, the people got the loan and so forth.

Mr. **Mansfield**. Or other recompense. We're required under title 8, sir, to attempt to conciliate all claims that are filed.

Senator **Dixon**. Well I don't have any problem with conciliation; I've always tried to be a conciliator myself, believe it or not. But do we ever find with some of these that somebody ought to be in some manner penalized to set some standards for the country?

Mr. **Mansfield**. Yes, sir. We haven't yet but I believe that we are on the road toward achieving that. And, as I said, through the individual complaint process where the numbers are, I believe, 35 in process right now, or through the Secretary-initiated investigation and complaint power that is given to me by the Secretary, I think we can move forward in this area and achieve results.

The idea of the Secretary-initiated complaint, in my mind, is to focus in different parts of the country and pick an area or an issue, for example, advertising or fair lending, where we can use the headquarter's resources and the regional resources and move into an area but where we'll have more than just an individual impact or a regional impact, and that's the way we're planning to run that system.

Senator **Dixon**. Well we'll be following up on some of those things with you, Mr. Mansfield, and with others.

May I say that I'm going to call in at some time soon Mr. Ronald E. Wienk and see what he has to say about this, Mr. Herrmann.

Mr. **Herrmann**. Well I'd certainly like to get back to you, Chairman Dixon, with the facts from our point of view. Frankly, I'm shocked——

Senator **Dixon**. Well may I say that I will be entirely fair in that regard. I'm going to ask my staff to see if Mr. Wienk can come in here some time soon to present his point of view and you will have an opportunity, you or anybody on your staff, to respond to that.

But may I say also now I'm going to be looking around. If we find some aggravated cases around here that haven't been referred to Justice, I put you all on notice, we're going to start flopping some of those people in witness chairs around here and let them tell their story and find out what's behind all this. These numbers have got to get better. They have got to get better. I'm telling you now. Nobody's ever going to convince me it's OK out there when these numbers are this bad.

I thank you all for obviously doing more than last year and we will pursue it assiduously.

Thank you for coming here.

[Witness panel excused.]

Senator DIXON. Ladies and gentlemen, the second panel is Michelle White, housing specialist, Western Center on Law and Poverty, Los Angeles; Shanna Smith, representing the National Fair Housing Alliance and Toledo Fair Housing Center; Allen Fishbein, general counsel, Center for Community Change; and Calvin Bradford, representing the Chicago Fair Housing Alliance.

Would you folks be kind enough to come on up?

Well we're delighted to have you here and whenever you folks are prepared to go forward.

Ms. White, you're first up to the batter's box.

STATEMENT OF MICHELLE WHITE, HOUSING SPECIALIST, WESTERN CENTER ON LAW AND POVERTY

Ms. WHITE. OK. Thank you very much. I'm very happy to be here.

I have to confess that it's like being in a time warp. I am the former special assistant for civil rights with the Comptroller of the Currency and hearing Mr. Weink's comments certainly harken back to a previous time when similar conditions existed.

At that time, all the regulators were similarly concerned about housing discrimination and in the process of redoing procedures and things like that and had in place the capacity to analyze the loans to see what kind of patterns existed within the bank for certain types of terms, conditions, based upon the sex, the race, the marital status of applicants and they could analyze them on the basis of which loans were approved, turned down, withdrawn before and after the application had been processed.

And very little was done with that information. Very little is done now with the information. And those systems still exist, I believe, at OCC and the FDIC, the programs still exist, and that information is not routinely reported in any manner that I'm aware of. So you might tap into that source of information the next time your hearing comes up because it's certainly available.

We have found in the process of doing an analysis of the lending patterns in Los Angeles that looking to the HMDA information, even that HMDA information that's going to be available after the modifications go into effect, is not adequate to really determine the market that is available for lenders who wish to make loans within given areas of the city.

In fact, you have to look to the assessor information or the transfer of title information. That gives you a much broader background and a much broader feel for the market. And that way you pick up mortgage lenders, finance companies and all the other lenders that typically operate in black and hispanic areas. Then you can assess what the traditional lenders, the commercial lenders and the thrifts, are doing in comparison to those companies who are indeed active in the areas.

We have found in black areas—one study that was done in south central L.A., only 3 percent of the transfer of titles that occurred during a 14-month period were financed by traditional lenders. The rest of the lending was primarily done by finance companies. They, of course, have higher rates and often are unregulated.

Many housing scams come about as a result of the use of finance companies and we have found that many foreclosures take place and our clients lose their properties as a result of the unavailability of traditional lenders in black and hispanic areas.

In addition, another thing that struck——

Senator DIXON. Remind me to come back to that when we're finished hearing everybody, because I'm anxious to pursue that with you.

Ms. WHITE. OK.

Another thing that struck me about the testimony today was that a lot of training of examiners is going on. A lot of modification of the procedures that exist for examining banks and thrifts have taken place over the last few years. And, notwithstanding all of this, there are no cases referred to Justice, there are no cases in which damages are allowed for individuals.

I have reached the conclusion over the last few years that in large part the examining staff at the regulated agencies—within the regulatory agencies are not educable with regard to civil rights enforcement. They are not predisposed to do civil rights enforcement and what they are predisposed to do is safety and soundness. It's what they're most comfortable with and they ought to be permitted to do that.

Those persons who are indeed comfortable with civil rights enforcement and advocacy ought to be introduced into the process to do precisely that. I think it is a waste of time to continue to try to train people who are not susceptible to this type of training.

For that reason, I would recommend that HUD, the fair housing councils, the Center for Community Change and such advocacy groups be more involved in the whole process of analysis and allow individuals, once they have the results of HUD investigations or other neutral investigations, go into court on their own or seek other remedies outside the regulatory agencies, because I don't think they're going to find it there.

With regard to testers, the big discussion when I was with the OCC was whether they were even going to go outside the bank to talk to community groups. Now people are talking about the possibility of using testers. I am somewhat skeptical.

I think that the testing ought to be done by fair housing centers or by persons who are capable and trained now to do testing. Those groups already exist; there's no reason to reinvent the wheel on this. And I think we ought to defer to the agencies that have the capacity and have the skills to do it.

One of the regulators—and I can't remember who—referred to the fact that—Am I done? I'm sorry. I will defer at this point——

Senator DIXON. I wasn't that tough on the regulators; I'm not going to be that tough on the consumers. If you've got anything more to say, say it.

Ms. WHITE. OK.

One of the regulators referred to the fact that something didn't smell bad enough to be investigated further. I think that's the seat of the pants approach that most of the regulators take to this. And what I found in the course of my investigations or my consideration of files while at the OCC: those things that smelled badly to me never even occurred to examiners as being offensive. So I don't think that we can rely upon the examination staff to do the kind of job that's necessary to eradicate discrimination in lending in the United States.

On that, I will defer.

[The complete prepared statement of Michelle White follows:]

TESTIMONY OF THE WESTERN CENTER ON LAW AND POVERTY

SUBMITTED TO THE SENATE COMMITTEE ON BANKING

ON MAY 16, 1990

(REGARDING DISCRIMINATION IN LENDING AND THE ROLE OF FINANCIAL REGULATORY AGENCIES)

Prepared by

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The Western Center on Law and Poverty appreciates the opportunity to present testimony to the Senate Committee on Banking regarding the discrimination in lending and financial regulatory responses thereto.

The Center is the statewide support center for legal services field programs. We have offices in Los Angeles and Sacramento, California. The Center has been commissioned by the City of Los Angeles to study the lending patterns of financial institutions doing business in the municipality. The City intend to use the results of this study as a basis for enacting a link deposit ordinance designed to encourage lending institutions to meet the needs of the Los Angeles citizenry, including the low income and minority communities.

Michelle White is the housing and economic development specialist for the Center. She has a varied background related to lending issues. While in private practice, she has represented institutions accused of violating fair lending laws. She also served as the Special Assistant for Civil Rights to the Comptroller of the Currency. She now represents indigent clients seeking redress under the Equal Credit Opportunity, Fair Housing and Community Reinvestment Acts.

RACIALLY IDENTIFIABLE HOUSING PATTERNS IN THE LOS ANGELES

The City of Los Angeles has housing patterns which are readily identifiable on the basis of race. With some exceptions, Latinos live in East Los Angeles and Pacioma, African-Americans live in South-Central Los Angeles, Pacific-Asians in Little Tokyo, Chinatown, Koreatown and other areas, while Whites live in North Hollywood, Studio City, San Fernando Valley and other areas.

The City has been racially identifiable for many years. A significant majority of the 1980 census tracts reflect a 50-70% predominance of one race over others. Los Angeles was recently named one of the ten most segregated communities in the United States.

Nowhere is segregation more apparent in Los Angeles than in its low income communities. Over 90 percent of all low income areas in Los Angeles are minority neighborhoods. Black ghettos and barrios have become so concentrated that it has been estimated that, in order to achieve full racial integration, over three-quarters of all African-Americans and over half of all Latinos and Chicanos would have to move into Anglo neighborhoods. The Widening Divide-Income Inequality and Poverty in Los Angeles. The Research Group on the Los Angeles Economy. UCLA (1989).

INVESTIGATION OF COMPLAINTS CONCERNING LENDING PATTERNS AND CIVIL RIGHTS ENFORCEMENT EFFORTS BY FINANCIAL REGULATORY AGENCIES

Any assessment of financial regulatory enforcement activities is difficult because the process is cloaked in secrecy. When CRA ratings and other enforcement verification information becomes available later this year, the process will be subject to improved, albeit imperfect, scrutiny.

The following lending policies and practices which have been endorsed by the financial regulatory agencies are matters of great concern to civil rights advocates in California.

1. **Failure to Properly Investigate Complaints of Discrimination.** Approximately one month ago, Concerned Citizens of South Central filed formal complaint with the Office of the Comptroller of the Currency (OCC) concerning the marketing, by mail, of a new home loan product by a large national bank. The OCC responded, acknowledging receipt of the complaint. It stated that the complaint would be placed in the bank's CRA Public File and investigated during the next examination. The OCC did not state when the next examination was scheduled. The letter was unsigned.

Concerned Citizens is an advocacy group familiar with the fact that the allegations, if proven, constituted violations of ECOA, the FHA, CRA, as well as the state and federal Constitutions. The members were outraged that the complaint was handled in such a cavalier manner.

2. **Gerrymandering Service Areas to Exclude Neighborhoods of Racial Minorities.** The Committee for Accountable Reinvestment, a multi-ethnic coalition of groups from the Los Angeles area, challenged the CRA performance rating received by Mitsui Manufacturing Bank by the FDIC, partially on the basis that the bank had for years gerrymandered its branches' service areas to exclude the largest concentration of African-American and Latino communities in Southern California. The challenge also noted that $2 billion facility was openly soliciting deposits and routinely lending outside its branches' service areas on the strength of its parent holding company's $200 billion assets.

Although the coalition raised significant issues of differential treatment on the basis of race, for virtually all of the persons included in the branch service areas are White and virtually of the persons excluded are minorities, the examiners charged with investigating the issues raised refused to meet with coalition representatives until the Washington FDIC intervened. Once the examiners finally agreed to meet with coalition members, the regulators refused to allow the staff of elected City and Congressional representatives to be in attendance.

3. **Failure to Respond to the Home Mortgage Market in Minority Communities.** Between October, 1987 and December, 1988, 1328 single family dwellings were sold in South Central. Only 3 percent of these dwellings were financed by commercial banks, while 54 percent were financed by largely unregulated finance companies.

As a result of usurious interest rates and unscrupulous activities on the part of certain of these unregulated lenders, residents of South Central have been subjected to a much higher incidence of foreclosures and home equity scams than is evident in comparable White areas of the City.

Although the financial regulators have been put on notice of the differential lending patterns and the effects on the residents of South Central, there is no evidence of any effective measures being instituted by the regulatory agencies to increase lending by banks and thrifts in minority areas of the City .

4. **Failure to Supervise the Closure of Bank Branches.** Regulators have chosen not to supervise the closure of bank branches. This failure to supervise has special significance under ECOA and FHA, for it has resulted in vast portions of the Latino and Black communities becoming virtually devoid of banking services, while retaining and promoting more than adequate services in the White areas of the City. The regulators permit a further exacerbation of this disparity when they allow banks to employ a policy of "customer preference" when extending home mortgage loans. The effect is to prescreen out Black and Latino applicants because of the unavailability of bank branches in these neighborhoods.

5. **Use of Intermeidary Funds.** Certain financial institutions have contributed money to lending pools which are, in turn, administered by intermediaries. Some of these banking institutions have taken the position that participation in these pools is adequate to meet their CRA and ECOA responsibilities. These intermediaries provide only select types of loans and do not provide full banking services within communities. The result is that when intermediaries operate in minority neighborhoods, the residents continue to receive materially different, i.e. inferior, levels and kinds of banking services, for which these residents required to pay additional intermediary fees. To the extent that regulatory agencies continue to encourage the use of intermediary funds without assessing the effect on access to credit by minority communities, these agencies act in dereliction of their FHA and ECOA enforcement responsibilities.

6. **Absence of Rehabilitation Loans in Minority Areas.** Loans to rehabilitate properties and provide seismic reinforcement are virtually unavailable in the older sections of the Los Angeles where many Latinos and African-Americans reside. Too often banks insist that other funding sources be used to front the costs of rehabilitating older structures. Only upon completion of the seismic repairs are many traditional lenders prepared to provide reimbursement loans. Because most homeowners in minority communities cannot afford to front the cost of rehabilitating their dwellings or to assume the excessive costs associated with obtaining loans from finance companies, these communities have a high incidence of health and safety code violations and non-compliance with the City's seismic repair ordinance.

The practice of only lending on already rehabilitated or seismic repaired dwellings in older sections of the cities is considered fiscally prudent, and in this era of increased caution with respect to real lending may be applauded by regulatory agencies. The effect is devastating, however, on the Black and Hispanic communities of Los Angeles. The regulatory agencies must begin assess the effect of the lending practices they permit and promote, especially in light of the increased inaccessibility of housing for minorities and the poor in urban areas.

7. Appraisal Practices. Residents in African-American and Latino sections of Los Angeles often complain that their residences are routinely underappraised. This complaint has a double edge, for to the extent that values in minority areas are equalized, housing costs become even more unaffordable in Los Angeles. Black and Hispanic homeowners in Los Angeles should not be the only residents expected to hold the tide against inflation, however. To the extent that the bank regulatory agencies permit financial institutions to rely upon appraisals which contribute to discriminatory lending patterns, these agencies must alter their practices.

8. Overreliance Upon Real Estate as Security. Residents of minority neighborhoods in Los Angeles complain that the limited number of financial institutions which are prepared to lend in Black and Hispanic areas will only accept real estate as security. In those instances in which real estate is generally not used to secure transactions, the financial institutions are being overly prudent, and should be discouraged from doing so by the regulatory agencies.

PROPOSED SOLUTIONS TO THE FAILURE OF REGULATORY AGENCIES TO PROVIDE ADEQUATE CIVIL RIGHTS ENFORCEMENT

The financial regulators view themselves as management consultants to financial institutions. Most examiners closely identify with the facilities they regulate; many expect to move into banking positions upon leaving their agencies.

As management consultants, examiners view their mission as insuring that their facilities remain "safe and sound" and operate within the law. In those instances in which a bank or thrift is out of compliance, the examiner's role becomes one of assisting management in achieving compliance.

These "consultants" and their financial institutions have traditionally operated in an atmosphere of financial secrecy to insure that bank operations are not subject undue influences. As a result of early training, most examiners seek to shield the institution from all the but the most positive publicity.

After examiners had established a long tradition of management consultation with lending institutions they were asked to enforce consumer laws, including civil rights provisions. In many ways these new responsibilities were considered inappropriate by examiners, inconsistent with their traditional obligations. The examiners believed that these new obligations placed them in an adversarial role with institutions with which they had previously operated in a spirit of cooperation.

The examiners generally chose to approach the enforcement of civil rights laws in the same manner as they enforce other laws for which they are responsible. They protect the integrity of the financial institution, take those steps necessary to correct fragrant violations and, at all costs, seek to shield the institutions from adverse publicity and possibility of civil suits.

The prospects of substantially modifying the approach of financial regulatory examiners to the enforcement of civil rights provisions are not rosy. Serious attempts have been made by advocates within and outside these agencies to achieve this end. Examiners have been trained and retrained, given additional tools to assist them in finding discrimination and encouraged to seek careers in consumer law enforcement. None of these efforts have achieved the much sought after goal of establishing an effective enforcement program within the financial regulatory agencies.

It is now appropriate to abandon the efforts to reorient examiners in favor of training civil rights advocates in banking principles and allowing them more access to lending records. HUD investigators should be given more information on a routine basis. The results of HUD investigations should be routine given to complainants, so that they can make a more informed determination about the merits of their cases before filing suit.

The fair housing and other advaocacy communities are adequate to protect the civil rights of consumers, iuf they are given the tools to assess the lending patterns of banks and thrifts.

Senator DIXON. Thanks, Ms. White.
Ms. Smith.

STATEMENT OF SHANNA SMITH, REPRESENTING THE NATIONAL FAIR HOUSING ALLIANCE AND TOLEDO FAIR HOUSING CENTER

Ms. SMITH. My name is Shanna Smith and I represent the National Fair Housing Alliance. And actually I was much more optimistic when we were here in October, and I tend to be a very optimistic person. But listening to the examiners today was not very uplifting or encouraging for me.

The letter that was sent out by the Federal Reserve Board was sent out May 9 and it's a very general letter. And my concern with asking those of us in the private fair housing movement to refer complaints to any of the regulators is that they have no enforcement powers, nor have they ever exercised the power that they do have.

It is in our clients' best interests and the interest of eliminating mortgage lending discrimination to go through the Federal District Courts and the Department of Justice.

I wasn't as hard on HUD as I feel toward the regulators because I know HUD is learning how to do this and they've just started this. My concern with HUD though is—and it is my experience in the cases that have been filed—is that their staff needs a lot more training on how to identify discriminatory practices.

We and the Toledo Fair Housing Center settled a case because we didn't feel the HUD investigator had a handle on understanding the complex issues that were raised in this case. The old Federal Home Loan Bank Board had already conditioned an application of the particular lender at issue, yet the HUD staff person was saying to us that she did not see any discriminatory conduct. She did not review the FHLBB's ruling.

However, there are other HUD staff people who are very good at investigating mortgage lending complaints. They know how to do a statistical analysis, they know how to look at credit reports and appraisal reports. Within the Department of Housing and Urban Development, we are finding that they are attempting to train the field investigators to understand the complexities of mortgage lending. The HUD staff is predisposed to investigating complaints from a civil rights perspective.

I must say that I see absolutely no conflict between the safety and soundness issues and promoting fair lending. And I continually hear a subliminal message from the regulators that if they promote fair housing that somehow it's going to undermine the safety and soundness of a bank. And that's not true.

None of us are promoting risky loans. What we're promoting is fairness. And I think——

Senator DIXON. I'm glad you made that point. Let's make that again. Nobody is trying to tell anybody to make a bad loan.

Ms. SMITH. That's correct.

Senator DIXON. What we persist in is the fact that there are plenty of absolutely good loans out there that are not being made to black men and women in America.

Ms. SMITH. Yes.

And the 15 or so lawsuits that have been filed in Toledo, OH, demonstrate that these were creditworthy individuals attempting to secure financing for homes that were in a variety of neighborhoods but mostly in well-integrated or minority neighborhoods.

And what so disturbs me—is that the regulators—and bank examiners don't recognize lending discrimination. Their own handbooks say that they're not allowed to have minimum loan amounts and that that could be indicative of discrimination; yet, those minimum loan amounts exist. You heard one of the regulators testify that a high minimum loan amount could have a disparate impact on minorities. Any minimum loan amount, depending on what city you're in, can have a disparate impact on Hispanics and African Americans.

Another issue is the private mortgage insurance. The lawsuit against the United Guaranty Residential Insurance Co. which challenged minimum insurance amounts was settled; they're the fourth largest PMI company in the country and they agreed to eliminate this policy nationwide.

And my understanding is that NTIC did a survey after that lawsuit was settled and United eliminated their minimum insurance policy nationwide, but in other companies this policy was still in effect. It would seem to me that the regulators should have issued some notice throughout the industry that minimum insurance policies, minimum loan amount policies are discriminatory and should be eliminated. I have no evidence that that occurred. The FTC, however, would be who we would complain to about PMI coverage.

The issue of testing is very important to us. There is testing going on currently in the United States against financial institutions: The prescreening and prequalifying testing. The difficulty comes when attempting the full-application testing, and some of us intend to do this tape of testing.

The problem is on the application it says if we falsify the information that we could be charged with a felony. In testing—I've done testing for 15 years, and the Federal courts have said it's fine to develop a cover story and to disguise ourselves in ways that we need to to uncover the discrimination that's occurring.

We probably need something from your committee saying that if we do testing and we put false information down on an application that the Department of Justice isn't going to pursue us individually on that particular case.

But testing will be the way for you to see the individual acts of discrimination that occur. It's been very simple for lenders to regulators to say that this is complex and the discrimination happens in every level of the application process and we can't identify it. But if we have the opportunity and the funds available to go through the application process, then we can identify it for them and make referrats to HUD and DOJ.

As I said in my written testimony, I don't think that it's impossible for them to learn how to do it. I do agree with Michelle White that they ought to have a different career path for people who are specialists in civil rights issues.

In Toledo we have filed about 15 lawsuits which have all settled. We've prevailed in pretrial decisions—pretrial motions where the judge said—it looks like discrimination is occurring.

We've brought these cases before having access to comparable files, the credit appraisal reports and all the other information that the examiner has his or her hands on. Yet we were able to say this looks like a discriminatory practice, file a lawsuit, and then through discovery develop our case.

We were novices in this area, but we took courses in real estate appraising, mortgage bank financing. The lenders in Toledo let us come into their classes to teach us how to understand the system and we've gone through appraisal courses so that we understand what functional obsolescence means when it hits an appraisal report——

Senator DIXON. I know you'll tell me what it means some time. [Laughter.]

Ms. SMITH. And if we can learn to do that, I think that the regulators can hire people who can teach the examiner the same things.

And last, I would continue to encourage HUD to fund these efforts and that somehow we be protected while we're doing our testing from any legal ramifications should we discover discrimination, or should we not, during the testing process.

The last thing is that when they're going to look at the analysis of all this data, it is so very broad—and I've talked about this with Justice—that you're looking at a very broad picture in trying to come up with systemic pattern and trends.

But each individual case of discrimination is different. There may be a nuance in that case that caused that application to be rejected so it may not be a full trend. When people are intent on discriminating against a neighborhood or an individual, they will come up with—they'll go through that whole process and find the one weak link. And that weak link may be able to be applied to whites who have applied, too. So it sounds just extremely too broad to narrow it down and say well this is the cause of it.

And last I'm extremely offended by the implication that blacks are less creditworthy than whites that is being made by the regulators. It was——

Senator DIXON. You know, I must say that was sort of implicit in a lot of what I heard from the regulators.

Ms. SMITH. And I find it offensive.

Senator DIXON. I'd like to have you comment on that.

Ms. SMITH. Well the 15 lawsuits and some of the 35 cases pending at HUD are ours. And in those cases the creditworthiness, there may have been something on a credit report.

But we have been successful in finding whites who have worse credit or also may have an R-2 on their credit history. But most of my cases have been minority families who are creditworthy.

And in the Briceno lawsuit, they did have a credit problem: They were married at age 19, they were buying their house at age 22. They had their first child when they had no hospitalization. They had a debt of $5,000, which they were paying $50 a week on to pay that debt and not go into bankruptcy.

And what had happened was the lender, who was willing to make the loan, said to us this couple is a good credit risk: They didn't file bankruptcy, they did all these things the right way, they are a good credit risk. They have all R-1 credit in every other aspect except this hospital bill.

And yet it was the PMI company who turned them down using that credit, and, also, we believe that it was the location and the price of the property because it was under $30,000.

So when you're analyzing the HMDA, it seems like it's going to be too general—and Cal can probably address that better—but it will show trends. And that trend may be what the examiner can look for. But they need to look at individual cases and not just a 6-month period, because there may have not been any loans made in that area to make a comparison.

It's a very complex issue but if they go in and they know what they're looking for and if they follow their handbook—Good Lord, I was looking at their handbook, if they just followed some of the ideas that were written in their handbook, they could find acts of discrimination.

And people are not going to report it to the regulators because they cannot make the victim whole.

Senator DIXON. Because they can't what?

Ms. SMITH. They cannot make the victim whole.

Senator DIXON. Yeah.

Ms. SMITH. The penalties are not there——

Senator DIXON. Yeah.

Ms. SMITH [continuing]. And you asked about is it a deterrent. We have found in the fair housing movement that civil fines and penalties and large monetary damages is what changes behavior, not simply telling them don't do this again.

Senator DIXON. Yeah. Sad but true, I'm afraid.

Ms. SMITH. Thank you.

[The complete prepared statement of Shanna Smith follows:]

TESTIMONY OF SHANNA L. SMITH
REPRESENTATIVE OF THE
NATIONAL FAIR HOUSING ALLIANCE

Members of the Committee, my name is Shanna Smith and I am representing the National Fair Housing Alliance located in Washington, D.C. The Alliance is a private, non-profit corporation representing more than 50 private fair housing centers throughout the country.

The National Fair Housing Alliance was founded in 1988. The mission of the Alliance is to promote the achievement of "the policy of the United States to provide, within constitutional limitations, for fair housing throughout the United States." The Alliance believes that by vigorous, positive and focused action, we can work together to achieve fair housing through outreach, education, litigation, conciliation and research into the nature, extent and effects of housing discrimination.

The members of the National Fair Housing Alliance are dedicated to working to develop and implement strategies to reduce, and eventually eliminate, racially and ethnically segregated housing patterns and to make all housing accessible regardless of race, color, religion, sex, familial status, handicap or national origin.

This hearing is to focus on the progress made since October 1989 by HUD and the federal financial institution regulatory agencies for dealing with mortgage lending discrimination.

I will take in order the areas you asked me to address.

I. REGULATORS AND HUD EFFORTS TO DEAL WITH MORTGAGE LENDING DISCRIMINATION

I have not seen evidence of any substantive efforts on the part of the federal financial regulators. I have seen limited evidence that the Fair Housing & Equal Opportunity Division (FH&EO) of HUD is attempting to learn how to deal with lending discrimination complaints. I have no information about the HUD-FHA section making any effort to address fair lending issues.

The Federal Reserve System staff did call me and invite me to discuss over lunch what type of complaints we investigate and how testing the industry might work. Then on May 9, 1990, the Federal Reserve sent letters to the private fair housing centers providing them with sketchy information about complaint procedures and asking the centers to direct complainants to the Board of Governors.

Since the other regulators did not contact the Alliance, then one could say the Federal Reserve made an effort. Technically this is true.

But is this evidence of a sincere effort to address one of the most serious problems facing America's minority and integrated neighborhoods -- **DISINVESTMENT** -- and the consequences of disinvestment which include abandonment, absentee ownership, loss of affordable housing stock . . . . flight from the neighborhood and the resulting impact on neighborhood schools?

I am afraid these actions are merely a window dressing to attempt to please this Committee, but in no way is this a real effort to address lending discrimination.

HUD's FH&EO Division contacted the Alliance to conduct training on mortgage lending discrimination for three HUD Regions and the staffs of the states civil rights commissions in these regions. These workshops will discuss how to recognize lending discrimination, the methods used to investigating these complaints and litigation and conciliation strategies.

Under the Fair Housing Initiatives Program (FHIP), HUD provided direct funding to private fair housing centers to conduct investigations and testing in mortgage lending complaints.

These are important steps for HUD to take and certainly more substantive than those of the regulators. However, the private fair housing enforcement movement does not have confidence that HUD or the federal regulators have the capabilities to detect mortgage lending discrimination and, therefore, cannot make the referrals that these agencies request.

II. INADEQUACIES IN THE EXAMINATION PROCEDURES TO DETECT MORTGAGE LENDING DISCRIMINATION

In reviewing the compliance handbooks, one would expect that the bank examiners would be able to detect discriminatory lending practices and policies. The Feds handbook clearly explains what "effects" standards should be applied when conducting a civil rights examination and they identify discriminatory conduct.

For example, when reviewing underwriting guidelines it clearly states that "the examiner should be particularly aware of property underwriting criteria which can severely limit the amount and type of credit available in older, integrated areas. Such criteria include, but are not limited to:

- Minimum loan amounts which may be higher than the average cost of a dwelling in a given neighborhood."

The handbook continues, "In looking for "redlining" the examiner should first check for improper loan underwriting policies; then look for evidence of improper appraisal policies (conversely, evidence of steps taken by the lenders to assure the absence of such policies by instructions to appraisers, brokers, and dealers)."

Although these instructions exist, it is obvious to me that they are not employed during the examination procedures. In Toledo, Ohio we had lenders who had minimum mortgage loan amounts and some who even tiered the interest rate higher for loans under $30,000.00. The regulators never questioned these policies or evaluated the impact these policies had on the African-American and Hispanic communities in Toledo. These policies were only eliminated after the local Fair Housing Center identified them and prepared to challenge the institutions efforts to merge or branch.

Likewise, lenders are doing business with appraisers, secondary buyers and insurers who have policies and practices that limit or deny mortgage money in neighborhoods because of the racial composition of the neighborhood. Clearly, the handbook states that there is an obligation on the lenders part to give instructions to these groups that their guidelines are improper and have a disparate impact on minority and low/moderate income neighborhoods.

I have not found a lender yet who refuses to do business with secondary buyers, insurers or appraisers because of their policies. Instead we find the lenders blaming these other entities for their failure to be able to provide mortgages in minority, integrated and low/moderate income neighborhoods. But this blame is not translated into affirmative action on the part of the lenders or regulators.

The Bricano v. United Guaranty Residential Insurance Company lawsuit was settled with an agreement that United would eliminate its minimum insurance requirement nationwide. Are examiners looking to see if all private mortgage insurers have eliminated this policy? Do the examiners even know about this lawsuit? How are examiners briefed about the latest fair housing/lending decisions, settlements, agreements?

It seems clear that lenders have an affirmative obligation to do business with companies who do not use discriminatory policies.

Is there any documentation that examiners are requiring lenders to protect themselves from charges of discrimination based upon policies and practices of the companies with whom they conduct business?

Recently an examiner met with staff of a private fair housing center and asked vague questions about lending problems we identified in Toledo.

We identified a specific concern that we have seen on adverse action notices from private mortgage insurance companies. Several adverse action notices that involve properties in moderate income neighborhoods as well as applications from women give the following reason for PMI denial:

> "not granting insurance on any application under the terms and the conditions requested."

First, we want to know what this language means. Secondly, does the examiner look to see if this language is used primarily on notices involving lower priced homes or for female applicants? Thirdly, who is teaching the examiner to identify this kind of language for its Fair Housing Act implications?

If the examiner is suppose to find and correct violations of the Fair Housing Act and ECOA and fails to do so, when a private fair housing center or individual victim of mortgage lending discrimination sues the bank, should we also sue the regulator for failing to identify and eliminate the discriminatory practice or policy?

The lenders have for the most part hired Community Reinvestment Officers. I have conducted training for many of them in Ohio and found them to be uneducated about the Fair Housing Act and uninformaed as to what constitutes acceptable community reinvestment activities. In addition, the CRA Officers and the Mortgage Loan Officers are not communicating about their obligations under CRA or FHA. The CRA officers have not idea who their banks' secondary buyers are or whether they have policies that limit or deny mortgage loans.

III. IF THE EXAMINER FINDS A PROBLEM - WHAT IS CORRECTIVE ACTION

The policy statement of the Feds says that nothing in the statement will "preclude the use of administrative authority that the Board possesses to enforce these laws, nor limit the Board's discretion to take other action to correct conditions resulting from violations of these laws, nor preclude referral of cases to the Attorney General."

To my knowledge no cases have been referred to the Attorney General. This is no surprise since the regulators cannot find discrimination or in the instances they sight, they believe that their corrective action makes a victim of discrimination whole.

The Fair Housing Act 42 U.S.C. 3608, section 808 (d) states:

> All executive departments and agencies shall administer their programs and activities relating to housing and urban development (including any Federal agency having regulatory or supervisory authority over financial institutions) in a manner affirmatively to further the purpose of this subchapter and shall cooperate with the Secretary to further such purposes.

Where is the coordination between HUD and the Feds and the Department of Justice? Is it possible that the regulators will not refer complaints to HUD or Justice because they are "user-funded"? What are the rights of the victims when they are identified by the regulators? Are victims advised about their fair housing rights and remedies under the federal Fair Housing Act?

The deterrent to continued discriminatory behavior has proven to be significant monetary damages: compensatory or punitive or a combination of both.

Yet, the regulators cannot, do not, or will not seek these remedies or refer cases to HUD or Justice so they can use the full force of the Fair Housing Act to change discriminatory practices.

Therefore, requesting the private fair housing movement to refer lending complaints to agencies that have demonstrated a lack of commitment and capability to even identify lending discrimination is futile.

Although we find the Department of Justice to be somewhat conservative, we know the staff possesses the capability and commitment to ferret out discriminatory practices and policies by lenders and private mortgage insurers. (Justice filed an amicus curiae brief in the Briceno complaint.)

As new as HUD is in locking into lending complaints, we know that at least in Region V, they have staff capable of conducting investigations of mortgage lending complaint.

The private fair housing movement, however, continues to be in the forefront in uncovering and challenging discriminatory lending practices.

Somehow this seems backwards. We do not have access to the files, loans registers, credit reports, etc., yet, we are the ones identifying these practices that deny lending and reinvestment opportunities to minority and integrated neighborhoods and minority and female applicants. We are the ones eliminating policies and securing affirmative relief and damages for victims.

How is it that we possess these skills and examiners do not? The difference may be as simple as the fact that we are civil rights experts. We have taken courses in banking, finance, appraising, underwriting, and insuring in order to understand the functions of these areas. Then we applied our fair housing experience and the civil rights statutes to lending practices and policies to identify barriers to equal lending opportunities.

We then proceeded to use the full remedies available under all regulations and statutes to secure settlements that made the victim whole for the act(s) of discrimination and worked with the lender to implement systemic policy changes designed to increase lending to qualified borrowers.

What use is a remedy that simply offers another application when the borrower found other financing? Does reducing the interest rate to that which the borrower was entitled to in the first place guarantee that the problem won't recur? Does it compensate the victim for the act of discrimination? The federal courts have said that a victim is entitle to compensation for the loss of his/her civil right. Where is that compensation in the regulators "corrective action"?

Accountability, I do not see it when it involves the regulators.

V. NEW DEVELOPMENTS IN MORTGAGE LENDING DISCRIMINATION

The wave of the future appears to be that lenders will contract with major grocery store chains and open offices in the new "SuperStores". In Ohio, these SuperStore lenders will offer a full range of services including the opportunity to apply for a mortgage loan. In Ohio these SuperStores are not being built in the inner cities, older neighborhoods or integrated neighborhoods.

Are the regulators considering what "effect" this practice will have on reinvestment, mortgage lending, full service banking privileges to those of us who do not live in the suburbs?

Discrimination will grow ever more subtle as Justice, HUD and the fair housing centers bring more litigation on behalf of individuals, neighborhood groups and the results of testing.

This will require increased sophistication on the part of all federal, state and private agencies charged with enforcing and monitoring the fair housing laws.

We can predict this increased sophistication because this is exactly what happened when the private fair housing movement began investigating rental managers and real estate companies. Some companies simply stopped engaging in discriminatory conduct because it was not worth the costs. Others, however, developed "legitimate business reasons" for denying minorities access to rental units. Real estate agents perfected "racial steering" skills to limit housing choices.

Fortunately, there will always be managers, real estate agents, lenders and insurers who want to practice the spirit and intent of the Fair Housing Act. They will continue to be the ones who point investigators and examiners in the right direction to detect and eliminate discriminatory practices.

The question is 'When will the regulators get into the game?" Will they continue to be part of the problem or part of the solution?

VI. RECOMMENDATIONS FOR ELIMINATING MORTGAGE LENDING DISCRIMINATION

A. In addition to the recommendations made in October 1989, I would strongly encourage the regulators to create positions for examiners who are first and foremost civil rights specialists.

Their job responsibilities would include monitoring practices and policies of lending institutions for compliance with the requirements of the Fair Housing Act, Civil Rights Act of 1866, Community Reinvestment Act, and the Equal Credit Opportunity Act.

Their educational and training requirements would include courses in banking, finance, appraising, underwriting and insuring of property and the fair lending implication under each of these categories. They would have training from the staff of Justice, HUD and private fair housing practitioners and lawyers on fair housing/lending investigations and litigation.

These requirements are not meant to be all encompassing, but a starting point to develop personnel who will be effective in meeting the intent of Congress to eliminate housing discrimination.

This same requirement and "specialist" should also be part of HUD's investigative team in FH&EO as well as in the HUD-FHA Division.

B. Require bank examiners to refer all complaints of mortgage lending, refinancing, home equity or insuring discrimination and any real estate related transaction where discrimination is alleged to both the Department of Justice and HUD's Fair Housing and Equal Opportunity Division. Referrals would include not only the complaints, but any and all information obtained during an examination that might indicate disparate treatment or potential violations of the Fair Housing Act and Equal Credit Opportunity Act.

C. Establish a Systemic Complaint Investigation Unit within HUD Headquarters to focus on two issues:

> a. Receive and investigate lending and insurance complaints. Lending complaints would include, but not be limited to, mortgage loans, homeimprovement loans, home equity loans, real estate related transactions and complaints involving the secondary mortgage market.
>
> Insurance complaints would include, but not be limited to private mortgage insurance companies, homeowners and renters insurance.

* This Unit would also have the ability to contract for "testing" of the industry for discriminatory pre-qualifying, pre-screening procedures and "test" the whole mortgage loan application process.

* This Unit could also contract for testing the policies and procedures for securing insurance including the PMI application, and application for homeowners/investment property insurance.

b. Commission fair lending/insuring audits to identify nature, extent and changes in discriminatory lending/insuring practices.

D. Require lenders to include a fair housing brochure explaining all the legal and administrative remedies available (both public and private) for any applicant who is rejected or the terms or conditions of their loan request are changed. This should written in a fashion that is easily understood and include telephone numbers for the Department of Justice and HUD FH&EO Division - Systemic Unit for questions or clarification.

When a private or public fair housing agency operates within the jurisdiction of the lender, the lender should also include information about that organization and a telephone number.

Senator DIXON. Thank you, Ms. Smith.

You're in a lot of trouble, Mr. Fishbein. A lot of these regulators say they're working with you to figure out how to solve this problem. What have you got to say in your defense?

Mr. FISHBEIN. Can you plead the fifth before this committee? [Laughter.]

STATEMENT OF ALLEN FISHBEIN, GENERAL COUNSEL, CENTER FOR COMMUNITY CHANGE

Mr. FISHBEIN. Good morning, Mr. Chairman. I'm Allen Fishbein and I'm general counsel of the Center for Community Change. And I want to commend you for having the stick-to-it-iveness to have this round of follow-up hearings which I think history has shown that that kind of prodding is absolutely essential to see any improvement in enforcement practices.

At last October's hearing, which I had the privilege to testify before, I testified that the agencies seemed to lack either the wherewithal or the will to use the full scope of their supervisory powers to enforce the fair lending laws and, sadly, we've seen very little evidence in the past 6 months that anything of a real substantive nature has changed.

Encouraging the formation of mortgage review boards is not going to address this problem. That is an idea that has been tried many years ago and is found to have a very spotty record.

I was listening to the regulators this morning elaborate on, you know, the various procedures they have for detecting problems and the examination techniques they use and all——

Senator DIXON. Well they're certainly testifying better this year.

Mr. FISHBEIN. They're doing their homework.

And they still never turn anything up. And I kept thinking about remember the Maytag repairman, remember that advertising campaign? It showed——

Senator DIXON. Sitting there all alone——

Mr. FISHBEIN [continuing]. To testify about the strength of his product, the repairman sitting by a phone waiting to hear a complaint about a Maytag washing machine and, of course, the phone never rang and he just slept and slept and slept.

And that's what it sounds like is going on here is the regulators are sleeping and sleeping and sleeping. They're not expecting to hear anything and I think, as Shanna and the other witnesses have testified, in large part that's because they don't really know what to look for.

Now you indicated that they have been showing some progress and some of it may be just better testimony but we pointed out in our written testimony that in some very concrete ways recent regulatory actions they have taken have really limited the usefulness of the fair lending information that is required to be reported under last year's FIRREA legislation. And I think that's an indication of mindset as much as anything else. And in our written testimony we discuss the series of reforms.

What I want to focus on today is testing and that technique and what it can do. The examination process that the banking regulatory agencies use, by their own admission, cannot detect the problem of prescreening, of discouragement of potential applicants before they actually submit an application.

I think the real story behind some of the research that the Atlanta Journal Constitution has obtained has not been just the higher rejection rates for minorities, but when you look at the number of applications received, there are far fewer applications from minorities than there are from whites. And part of the reason may be the result of this prescreening and discouragement.

Testing is an investigative technique that's been upheld by the Supreme Court to be a valid technique for spotting discriminatory lending practices. And in it what you do is you fabricate the identity of borrowers who go in and ask for information from a lending institution. And they are equal in all respects. They have the same type of house that they're seeking to purchase, the same income levels, the same employment history, you can construct any scenario you want. They have one spouse and two kids or however you want to do it. The only difference is their race.

And we were asked by a State human rights agency—and this was referred to in the HUD testimony—to design a testing program that could be used to spot this very problem of prescreening and discouragement at what's called the preapplication or loan origination stage. And the results of our project we feel show that this can be—testing can be a very effective technique for spotting problems.

What we found through this project is differential treatment between minority testers and white testers in how they were treated by loan officers. But often it was around how to qualify for credit, as much as anything else.

We didn't find lenders, for example, trying to charge a higher interest rate or more points for a minority who came in the door than a white, but it was the kind of information and how cooperative they were with working with the testers that often was the telling difference.

Now just to give you a few examples of that, of what we found, a black tester was told by a loan officer in one case that the institution does not interview for mortgages at this particular location and they'd have to go to another location.

A white tester comes in the door—same circumstances, equally creditable by a lender's own underwriting standards—and they're told they're in the right place and they were given information about conventional loans.

Another example: A black tester comes in the door, told by the loan officer that they talked to based on the information they provided them that they might qualify for the loan, it was hard to tell, the lending process was complicated and that they actually might qualify for an FHA loan. And these testers were going in and seeking essentially conventional credit.

But they were told that they might qualify for an FHA loan and they were given the name and phone number of another lender to go to who was specializing in FHA lending.

The white tester comes in to the same institution, FHA is never mentioned to the white tester and they're encouraged to apply right on the spot.

Senator DIXON. If I could interrupt there—and I don't want to make this a practice—now at that preliminary stage, I'm wondering what you're saying we could do about that.

I hear what you're saying. These are all those practical things that one can do to discourage initially the pursuit of the application for a loan. That's the point you're making; it's a valid point. I'm sure everyone in the room understands it.

But how do we do something about that? That's a little—it's insidious certainly but it's also kind of hard to figure out how you solve that. I wondered what your observation is about that.

Mr. FISHBEIN. Well the testing——

Senator DIXON. I mean you haven't refused a loan or anything yet here, have you? You're discouraging——

Mr. FISHBEIN. Well and that can be an illegal activity in and of itself, that discouragement of an individual——

Senator DIXON. Could there be a remedy for that, in your view?

Mr. FISHBEIN. Yeah, under the Fair Housing Act that would be considered illegal treatment——

Senator DIXON. Would money damages lie? I mean, could you——

Mr. FISHBEIN. Potentially. Potentially.

And it also could be an investigative technique that would allow fair housing agencies, HUD, the banking regulatory agencies, to go even further and perhaps examine the loan application files of an institution and perhaps discover other examples of discriminatory practices as well.

Senator DIXON. I have to tell you as a lawyer that if you stop there it's a fairly tough case, I think. Although maybe there have been cases made on that. I get the point.

Excuse me for interrupting you, Mr. FISHBEIN. But you're the expert here everybody has referred to, I've got to find out——

Mr. FISHBEIN. And I can go on and on with these examples. But what was clear was that there was a whole different aura and procedure that a number of different loan officers would use with black testers than white testers. And often those were the critical pieces of information that were needed in order for that person to qualify.

I'll give you one more example. A black tester was told basically the rules are not the exception. They were told that if they made a 10 percent downpayment, the bank required them to provide the equivalent of six mortgage payments to be deposited in the bank.

Now the white tester was told the same thing, but it was also added that if they put 11 percent down, they would need only a cash equivalent of two and not six mortgage payments.

So we found a pattern of this activity, quite extensive, and we think this would have a very useful application. I think from the written testimony and from what the regulators said today, the reality is they are unlikely to engage in any serious way in testing themselves.

And so the decision becomes if testing is going to be used as a systematic investigative technique, it has to be housed under the auspices of another agency, and we feel that HUD has at least the most experience in some aspects of testing, particularly in sales and rental, and that they ought to be directed to undertake a major testing effort which would involve engaging private fair housing agencies and public agencies to do testing for lending discrimination in the local communities where these organizations were located.

And that would be the singlemost telling way of getting at this problem of discouragement, prescreening, which is distorting the mortgage lending process and ultimately making it more difficult to spot patterns and practices of lending discrimination.

[The complete prepared statement of Allen Fishbein follows:]

center for community change

TESTIMONY BY

ALLEN J. FISHBEIN
GENERAL COUNSEL

CENTER FOR COMMUNITY CHANGE

WASHINGTON, DC

on

MORTGAGE LENDING DISCRIMINATION AND FAIR LENDING ENFORCEMENT

before

THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING AND CONSUMER AFFAIRS

UNITED STATES SENATE

May 16, 1990

1000 WISCONSIN AVENUE N.W. WASHINGTON, D.C. 20007 202/342-0519

Summary of Testimony

At last October's hearings before this Subcommittee, I testified that the federal banking regulatory agencies lacked the will or the wherewithall to use the full scope of their supervisory authority to combat racial discrimination. Although the agencies point to several minor steps they are studying to improve their enforcement capabilities, very little appears to have changed over the six months since the first set of hearings were held.

Recently promulgated regulations implementing changes to the Home Mortgage Disclosure and the Community Reinvestment Acts indicate a lack of sensitivity as to what is needed to detect discriminatory mortgage lending practices. In three key respects, the banking agencies regulations unnecessarily limit the loan data that will available to the public:

o Federal Reserve Board regulations adopted last December exclude the overwhelming majority of mortgage and home finance companies from having to report on their mortgage lending practices for fair lending enforcement purposes. The Fed argues they were merely interpreting statutory language, but the provisions sponsor Rep. Henry Gonzalez, Chairman of the House Banking Committee, has written to the Board of Governors disagreeing with the restrictive way in which the regulations were applied.

o The new HMDA regulations require lenders to maintain information about each application they receive on a Loan Application Register and to send these reports annually to the regulators for further analysis. The regulators initially indicated they would not make the LARs available to the public, but backed off in the face of community group and congressional opposition. Now, the regulators are refusing to release certain types of information contained on the LARs, which fair housing groups believe is critical to detecting discrimination.

o The regulatory agencies recently issued uniform guidelines describing the procedures they will use for disclosing CRA ratings and evaluations to the public. Under the guidelines, lenders will be rated separately in five performance categories and assigned an composite rating based on these evaluations. Unfortunately, these guidelines will permit examiners to assign satisfactory or higher ratings to lenders, even if they have violated fair lending laws.

We are proposing a five-step program to reform the fair lending enforcement. The features are as follows:

1. Using Testers to Detect Discrimination In Mortgage Lending.

The examination process is the basic tool the banking regulators use to detect illegal discrimination. In practice, the agencies have found no or virtually no instances of discriminatory behavior among the institutions they supervise. However, even at its best, the exam process as currently structured cannot uncover pre-screening, or the illegal discouragement of applicants on the basis of their race, sex, or national origin, or the racial characteristics of their neighborhood, since it does not leave the paper trail necessary to allow detection by examiners. Clearly, additional procedures are needed.

Testing is an investigative technique that has long been used to discover discrimination in the housing sales and rentals. Matched pairs of testers are used (minority and non-minority) to determine whether a landlord, realtor, or lender is using differential treatment. The use of testers has been upheld by the U.S. Supreme Court.

Based on a demonstration project we supervised, we believe that testing can be used to detect discrimination at the pre-application or loan origination stage. In order words, we found differential treatment in the way in which Black testers and White testers were treated. Often this involved withholding certain important information about "how to qualify" to Black testers. These tips are often critical in receiving loan approval.

The regulators are unlikely to sponsor testing. Consequently, HUD should be directed to develop a major mortgage lending testing initiative and contract with local fair housing organizations and public agencies to test for discrimination in this field.

2. Appraisal Reports Should Be Available to Home Loan Applicants

Fair housing advocates have long held that under-appraisals are used as a method for rejecting an applicant seeking a mortgage for property located in a minority neighborhood. Unfortunately, most lenders treat the appraisal reports as their own property and will not share the information with the applicant (even though the applicant has paid for it). As a result, applicants do not have access to the information and cannot contest incorrect appraisals.

We support legislation that would guarantee the applicant's right to obtain a copy of his or her appraisal report. The release of this information would go a long way toward discouraging appraisers and lenders from engaging in discriminatory practices in the way in which they estimate property values.

3. **Fair Credit Reporting Act Should Be Amended To Permit Credit Agencies to Support Testing Efforts.**

The credit check is an important part of the loan approval process. While lenders have little control over the information they receive, how they use this credit information can lead to differential treatment for minorities. For example, lenders must decide under what circumstances to allow exceptions to perfect credit records. Differential treatment by race can occur in the way lenders make exceptions, or under what circumstances they permit explanations.

An obstacle to testing throughout the mortgage loan process is the inability to fabricate credit histories. A fabricated credit history would enable a testing project to explore whether a lender treated certain credit histories differently. Credit bureaus are reluctant to cooperate with fair housing agencies in the view of the lack of expressed authority to do so.

Amending the Fair Credit Report Act to authorize this type of activity would greatly facilitate the ability to use testing to detect discrimination.

4. **The Non-discrimination Regulations For S&Ls Should Be Extended to All Mortgage Lenders.**

Currently, only the Office of Thrift Supervision has regulations to specifically bar lenders from engaging in discriminatory loan practices prohibited by the Fair Housing Act. The regulations also permit homebuyers to obtain copies of the underwriting policies used by savings institutions.

We recommend that these regulations be extended to commercial banks, credit unions, mortgage companies, and anyone engaged in the business of mortgage lending.

5. **Establish Separate Fair Lending Compliance Divisions Within the Banking Regulatory Agencies.**

Currently, only the Fed uses as separate division to conduct fair lending compliance exams. Meanwhile, the Fed is moving toward this approach.

We recommend that the Office of the Comptroller of the Currency, which regulates national banks, and the Office of Thrift Supervision, which regulated savings institutions, be required to establish separate fair lending compliance divisions. The chiefs of these divisions should be able to report directly to agency head to ensure their independence from the other examination functions.

Good morning, Mr. Chairman and members of the Subcommittee on Consumer and Regulatory Affairs. My name is Allen J. Fishbein. I am the General Counsel of the Center for Community Change and also direct its Neighborhood Revitalization Project. The preparation of my written testimony was assisted by Deborah Goldberg, the Project's Reinvestment Specialist.

The Center is a national non-profit organization, based here in Washington, which provides research and technical assistance on a variety of housing and community development matters to community-based organizations representing low income and minority neighborhoods. Our work in the fair lending field spans over 15 years and includes the publication of several major studies, including **Opportunities for Abuse: Private Profits, Public Losses and the Mortgage Banking Industry (1977)** and **Response to Crisis: A Study of Public Policy Toward Neighborhoods and Fair Housing (1980)**. Our most recent study, **New Research Shows S&LS Shun Lower Income and Minority Neighborhoods**, was released last year. The study analyzed mortgage lending patterns in 14 cities and found that banks and S&Ls were more active mortgage lenders in non-minority areas than in minority areas.

Mr. Chairman, we commend you for holding these second round of hearings on the subject of mortgage lending discrimination. We have found that the watchful eye of Congress is an important means for ensuring that the banking regulatory agencies are paying sufficient attention to their fair lending responsibilities.

As you may recall, when I testified before this Subcommittee last October I stated that the federal banking agencies either were unable or unwilling to use the full scope of their supervisory authority to combat racial discrimination in mortgage lending. And indeed, the other fair housing advocates appearing before this panel that day voiced very similar criticisms about the regulatory agencies' enforcement practices.

Last Fall's hearings concentrated on the numerous studies of mortgage lending patterns in metropolitan areas which indicate that racial factors affect the flow of mortgage credit. The regulators admitted to being bewildered by the research results, but defended their existing approach to enforcement. In their testimony, several of the agencies indicated that were exploring a few new initiatives -- support for mortgage review boards, greater collaboration with each other, and greater reliance on consumer pamphlets -- all of which can be termed as a fairly minor response to the issues presented by the mortgage lending studies. One of the agencies, the Office of Thrift Supervision, noted that the agencies as a group were considering new enforcement tools, such as the use of testing and the employment of interagency "Swat" teams to eradicate any lending discrimination that may exist.

The U.S. Department of Housing and Urban Development was the one agency to acknowledge that it had not fully met its responsibilities in the past, through its failure to provide data on FHA lending activity under the Home Mortgage Disclosure Act. The agency also committed itself to upgrade the data available for fair lending enforcement purposes by requiring mortgage lenders it deals with to submit information on the race, sex, and income level of borrowers. We were also pleased to learn that HUD intended to give fair lending enforcement increased attention.

Well, Mr Chairman, it has been almost six months since these first hearings were held, not surprisingly the banking regulatory agencies are continuing to study the issue, and very little appears to have changed. What is worse, although the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) provided the agencies with an opportunity to enhance their fair lending authority, they are reluctant to fully utilize these provisions. Specifically, FIRREA mandated important changes to HMDA and the Community Reinvestment Act.

The changes to HMDA required collection and reporting of data on race, gender, and income characteristics of applicants for mortgage loans. The amendment to CRA requires the regulatory agencies beginning this July 1 to disclose the rating and written evaluations they assign to each lender they supervise. We had anticipated that implementation of these fairly specific statutory mandates would be quite straightforward, but unfortunately, we have not found this to be the case.

First, last December the Federal Reserve Board published rules implementing the statutory changes to HMDA. However, they did so in a way which exempted thousands of mortgage and home finance companies from the reporting requirement. The Fed did this by extending the $10 million asset threshold requirement for banks and savings institutions to non-depository mortgage lenders. The agency argues its was required to do so by statute, but the provisions co-sponsor, Rep. Henry Gonzalez, Chairman of the House Banking Committee, strongly disagreed with the Fed's interpretation of this provision. As a result, only about three dozen mortgage companies will be required to report under the new rule. The practical effect of this new rules is that it limits the ability of federal, state, and local enforcement agencies to monitor for fair lending from the smallest and least regulated segment of the mortgage lending industry. As it stands now, it will be virtual impossible to determine whether these lenders are engaged in discriminatory mortgage practices. lending industry.

Second, under the new HMDA regulation, lenders are required to maintain a Loan Application Register to record significant information about each loan application they receive. Analyzing the LARs can be extremely useful in monitoring for lending discrimination. Initially, the Fed refused to make the information contained on the LARs available to the public, but it backed off of this position in the face of public and congressional opposition. Unfortunately, it appears the Fed is continuing to balk at the disclosure of two important columns of information contained on the LAR. These columns pertain to the date on which the application was submitted and the date on which the final disposition was made. Fair lending advocates believe that disclosure of this information is vital since it will enable them to determine whether a lender takes longer to process a applications from a minority than a non-minority. The Fed argues this information is confidential and its must be withheld to protect the applicant's privacy. Yet, it appears to be unwilling to agree to an acceptable compromise which would provide the public with basic information about the number of calendar days that have elapsed between submission and final disposition. This compromise position addresses concerns about protecting the borrowers' privacy.

Third, we are disturbed by the way in which the recently published Uniform Interagency CRA Guidelines For Disclosure Of

Written Evaluations and Revisions To Assessment Rating System tend to minimalize mortgage lending discrimination issues. According to the agencies guidelines, examiners will rate lender performance in five categories: 1) Ascertainment of Community Credit Needs; 2) Marketing and Types of Credit Extended; 3) Geographic Distribution and Record of Opening and Closing Offices; 4) Discrimination and Other Illegal Credit Practices; and 5) Community Development. Based on the individual ratings a lender receives in each of the five categories, the regulatory agency will assign the institution an overall CRA rating, based on a four-tiered scale. Unfortunately, the guidelines as currently written do not automatically bar those lenders that are found to be engaged in discriminatory practices from receiving a satisfactory or higher CRA rating. In other words, a lender engaged in substantive violations of the fair lending laws conceivably still could receive a satisfactory CRA rating if it scored well in the four other performance categories. As a result, the agencies have squandered an excellent opportunity to enhance their fair lending authority. The automatic barring of those lenders engaged in substantive violations of the fair housing laws would have been a powerful new incentive for discouraging the continuation of discriminatory practices.

Based on these recent actions we are concerned that little has changed in the agencies' position on basic fair lending enforcement and they will continue to do as little as they can to address the issues posed by the mortgage lending studies. Meaningful reform will require congressional action.

For the remainder of testimony, I will concentrate on discussing five-step reform package we believe is necessary to upgrade fair lending enforcement.

1) Using Testing To End Discrimination At The Loan Origination Stage

The examination process is the basic tool the banking regulators use to detect illegal discrimination, at least with respect to depository institutions. In practice, the banking agencies have found no or virtually no instances of discriminatory behavior among the institutions they regulate. For many years, civil rights advocates and community leaders have raised questions about the adequacy of exam procedures, examiner training, and the amount of resources devoted to detecting and eliminating discriminatory patterns and practices, and whether enforcement action is taken by the agencies when discrimination is found.

However, even at its best, the exam process as currently structured cannot uncover pre-screening, or the illegal discouragement of applicants on the basis of their race, sex, or national origin, or the racial characteristics of their neighborhood, since it does not leave the paper trail necessary to allow detection by examiners. When pre-screening happens, the potential borrower never gets to the point of filing a loan application. Clearly, additional procedures not currently employed by the regulatory agencies are needed to uncover illegal pre-screening by financial institutions.

Testing

Testing is an investigative technique that has long been used by civil rights enforcement agencies to discover whether or not civil rights violations are occurring. Its used most frequently in connection with investigations into practices used in the fields of housing sales and rentals.

Let me briefly illustrate how testing works in the rental housing field. Two testers are matched for every relevant characteristic (i.e. family size and status, income, type and length of employment, and the type of unit sought). The only difference between the two testers would be the characteristics being tested - race, or sex, or national origin, etc. Usually the protected tester is given slightly more favorable characteristics, so that he or she is a somewhat more attractive candidate for the housing unit. The testers are then sent in, one after the other, to apply for the rental unit. They provide the landlord with the same information about themselves and the unit they are seeking, and carefully record their experience. When the two testers' experiences are compared, any differences in treatment can be attributed to the characteristic being tested. Generally a series of tests are conducted before any conclusions are drawn.

The use of testers has been upheld by the U.S. Supreme Court as a valid means for uncovering discrimination and a legitimate civil rights enforcement tool. The courts have even given testers who have experienced discrimination while involved in testing standing to sue and receive damages.

Applying Testing To Mortgage Lending

The application of testing to the mortgage lending field has been limited. However, based on our recent experience we believe testing can be a useful tool for detecting whether prescreening and illegal discouragement are occurring, based either on the characteristics of the borrower or the area in which the security property is located.

We were commissioned by a state human rights agency to develop a methodology for testing for mortgage lending discrimination purposes. There are a number of significant obstacles that make it difficult to use testing to determine whether discrimination occurs after the application has been filed. However, we found that testing at the pre-application or loan origination stage is fairly straightforward, for which fabricated identities commonly used in testing were quite satisfactory.

Ten testers - five White and five Black - were recruited for the project. Each tester (team 1 White and 1 Black) was assigned a house that they were "buying." All of these houses had been on the market in the recent past, but their listings had either been withdrawn or expired. We drew houses from three types of neighborhoods (predominately minority, racially integrated, predominately non-minority). This enabled the project to test for possible discrimination on the basis of the neighborhood's racial composition as well as on the basis of the race of the applicant.

Ten of the most active commercial banks, savings institutions, and mortgage companies were selected to be tested. Information on their lending volume came from data disclosed under the Home Mortgage Disclosure Act.

The project called for each tester to test each of the ten lending institutions selected, for a total of 50 tests (100 visits). In all, 85 visits were actually made (41 by Black testers, 44 by White testers).

General Findings

Because each institution offers somewhat different loan products and has different underwriting standards, comparisons of the way Blacks and Whites were treated were made only within each institution, not between institutions. Specifically, we looked at:

1. Whether the interviewer (loan personnel) was interested, informative and responsive;

2. Whether the interviewer was willing to recommend loan types (and the reasons for the recommendations);

3. Whether the interviewer gave "how to qualify information", or gave different facts to different testers; and

4. Whether the interviewer provided written information, using the testers' personal data on the forms (e.g., applications, prequalifying forms, good faith estimates, etc.).

We found that three areas of differential treatment of Blacks and Whites emerged. The most common was a lack of interest, or discouragement -- unwillingness to take or give meaningful information, unwillingness to pre-qualify applicant, and either discouraging or not encouraging them to come back to apply formally.

Second, we found that a common form of differential treatment was withholding from Black testers the "how to qualify" information, particularly the little secrets that can make the difference in qualifying (e.g., getting gift letters to meet downpayment requirements or filing an application right after pay day, when the applicant's bank balance is expected to be at its highest level).

Third, we found differential treatment through the way which loan personnel recommended a different loan type for Blacks and Whites. Sometimes all Blacks were directed to FHA loans, even when they wanted conventional loans. Sometimes Blacks (but not Whites) were directed to a loan type for which they did not qualify and would be likely to be turned down without "how to qualify" information.

Another hypothesis the project tested was that lenders might treat borrowers differently based on the racial composition of the neighborhood in which the house was located, a practice known as "racial redlining." To test for this, both halves of each pair of testers were assigned houses in neighborhood of similar racial composition (e.g., both testers had homes in either predominately Black neighborhoods, predominately White neighborhoods, or integrated neighborhoods).

However, the test results did not present a definitive picture whether racial redlining occurred. We found that with most lenders, the race of the tester appears to have been the factor influencing the treatment the tester received, and not the composition of tne neighborhood in which the house was located. We found we needed more tests to reach definitive conclusions on this point.

We believe the results of this project demonstrate that testing can be successfully adapted to the mortgage lending process. The results indicate that at the pre-application stage, discrimination can take the form of qualitative differences in treatment of minority and non-minority applicants. The differences can be subtle, involving either efforts to discourage minorities from applying or failing to give them the kind of help that Whites tended to receive and is needed to obtain a loan. The examination process cannot detect these types of problems.

As our experience indicates, the use of testing can be quite effective to determining whether lenders are pre-screening or otherwise discouraging minorities from applying for mortgage credit. However, the banking regulatory agencies do not feel comfortable with sponsoring testing and are unlikely to use this investigative technique on their own.

Accordingly, we believe that the authority for engaging in testing for mortgage lending discrimination should be assigned to the U.S Department of Housing and Urban Development, which has had some experience with the use of testing, largely in the sales and rental fields. HUD has expanded authority in the fair lending area as a result of the 1988 amendments to the Fair Housing Act.

We further recommend that HUD's Fair Housing and Equal Opportunity Office be directed by Congress to establish a program to contract directly with private fair housing agencies to test for mortgage lending discrimination.

2. Assuring Nondiscriminatory Appraisals.

The appraisal is used to estimate the value of the collateral. Fair housing advocates complain that under-appraisals are used as a method for rejecting an applicant seeking a mortgage for a property located in a minority neighborhood.

A lender will refuse to make a loan for more than some percentage of the appraised value of the property (usually 80%, and perhaps up to 95%). Thus, if the appraisal is for less than the selling price, the borrower will be required to provide a larger downpayment in order to receive financing from the lender. Even if the appraisal is not under the sales price, a borrower receiving a low appraisal will have to make a larger downpayment in order to keep within the lender's underwriting guidelines. This would occur if the appraiser found conditions that warranted lending for less than the loan to value it underwriting standards permitted.

Most lenders treat the appraisal report as their own property and will not share it with the applicant, even though it is the applicant who has paid for it. Accordingly, the applicant normally does not have access to information and therefore, cannot contest how the value of the property was determined (i.e. the location and condition of the properties that were used as comparables, financial adjustments that were made to reflect variations in the comparables, the reasons for those adjustments, and judgments about the economic life of the property).

We urge the Subcommittee to adopt legislation guaranteeing the applicant's right to obtain a copy of the appraisal report on the property he or she is seeking to purchase. In fact, we cannot think of a valid reason for not making this information available.

After all, the information the appraisal is based upon is derived from information that is publicly available (e.g. recent property transfers, their sales prices, and frequently information about the mortgagor and mortgagee) through the local Recorder of Deeds Offices, local realtors, and even the newspaper. It seems to us, that if the appraisal reports are valid, neither the lender nor the appraiser should object to its being shared with the applicant. It should be noted that the National Credit Union Administration requires credit unions to make appraisals available upon the borrower's request.

In short, there is no quicker way to end discrimination in appraisals than to get potentially discriminatory appraisals into the hands of the borrower and the real estate broker. The sooner the information is required to be made available to the borrower, the sooner discrimination in appraisals will be ended.

3. Amending the Fair Credit Reporting Act To Facilitate Testing

Along with the appraisal report, the credit check is a very important part of the loan approval process. It provides the information that enables the lending institution to determine the likelihood that the loan will be repaid in a timely fashion.

Lenders receive credit information from three sources: 1) order a report from a local credit agency; 2) order a report from one of the three big credit bureaus -- CBI, TRW, or the Credit Bureau of America; 3) order a report from a credit verification firm which will gather information from one or more three sources and then verify its accuracy. The type of credit check a lender does often depends on whether or not it intends to sell the loan to a secondary market investor.

Lenders have little control over what information they receive through a credit check. It is how they use the information that may lead to differential treatment for minorities. For example, while lenders may prefer perfect credit histories, they may allow for exceptions to perfect credit (e.g., permit opportunities for borrowers to provide written explanations for exceptions to otherwise good credit histories).

Differential treatment by race can occur in the way lenders do or do not make exceptions, or under what circumstances they permit explanations for credit problems.

One of the major obstacles we found to testing throughout the application process is the credit report. Neither local nor national credit agencies are likely to cooperate with testing programs without express authority to do so. For example, these agencies could be quite helpful to the testing process by working with duly authorized agencies to fabricate a testers credit records. Amending the Fair Credit Report Act to expressly authorize this activity would greatly facilitate the use of testers in the actual mortgage loan process.

4. The Current Non-discrimination Regulations for S&Ls Should Be Expanded To Include All Mortgage Lenders.

To its credit, the Federal Home Loan Bank Board and now its successor, the Office of Thrift Supervision, is the only regulatory agency to have adopted non-discrimination regulations.
These regulations, among other things, prohibit savings institutions from refusing to consider loan applications on the basis of the age or location of the dwelling, and from discriminating based on race, color, religion, sex, or national origin, in fixing the amount, interest rate, duration, application

procedures or other terms or conditions of housing related loans. These rules operate in addition to the provisions of the Equal Credit Opportunity Act (Reg B). The regulations also prohibit S&Ls from relying on discriminatory appraisal and underwriting standards.

Moreover, the OTS regulations require S&Ls to have written loan underwriting standards, which are available to the public upon request. This provides loan applicants, fair housing groups and public agencies with a means to measure actual practices against the professed institution wide standards to determine whether differential treatment exists.

The banking agencies never adopted non-discrimination regulations. When they were adopted by the thrift regulator, the banking agencies claimed commercial banks were not a significant part of the mortgage market and therefore, detailed non-discrimination regulations were not needed. Obviously, times have changed. Overall, commercial banks originate more mortgages than does the withering S&L industry.

Non-discrimination regulations would help to clarify the regulators authority to prevent geographic redlining, the practice whereby a lender may arbitrarily discriminate against properties located in certain neighborhoods the institution deems to be undesirable.

Non-discrimination regulations should also be adopted by HUD, the Veterans Administration, and the Federal Trade Commission (which has residual authority over lenders not supervised by the other regulatory agencies).

5. Establish Separate Consumer/Fair Lending Examination Division Within Each Of the Banking Regulatory Agencies.

We have long advocated the need for developing a separate specialized examination division for fair lending, CRA, and consumer compliance. The divisions would have the responsibility for conducting these examinations, using a staff a trained specialists in these areas.

Most importantly, these consumer divisions would report directly to the head of the agency. The division would also make recommendations on pending bank expansion applications based on the CRA/fair lending/ and consumer compliance records of the applicant institutions and its subsidiaries.

At the present time, only the Federal Reserve Board uses separate consumer compliance specialists to examine the banks its supervises. In the testimony it presented last October, the

Fed spoke very positively about the need for specialization in this areas in view of recent developments.

In addition, we hear that the FDIC is converting to a specialized consumer exam as well. We view this as a positive development. However, it must be emphasized that unless the chief of this division has the authority to report directly to the agency head, which does not now happen even at the Fed, the thrust of these separate examinations are likely to buried within the overall examination function.

This concludes my formal testimony. I will be glad to answer any question the members of this Subcommittee may have.

Senator **Dixon**. If I may depart from the usual scenario one more time before I go to Mr. Bradford.

I sense by now that's the general feeling among consumer groups, that the best place for this is HUD. Am I getting the right message here?

You don't agree?

Mr. **Bradford**. HUD has that responsibility, but it's been my experience in working on these issues since about 1972 that HUD is one of the major discriminators in the area of fair housing. And one of the recommendations we make is that, in addition to whatever responsibilities HUD has, that there be an independent review board created to monitor the fair lending practices of the reg agencies, HUD and the Veterans' Administration, and report to Congress on its findings.

Because, it hasn't been effective in the past to put one of the agencies that has been one of the worst offenders in charge of these activities. They do have the authority and I think under Secretary Kemp they have much more willingness than they've had in the past.

Senator **Dixon**. Well I was almost tempted to pursue that, whether this was—You get around here these responses that let's not have a line-item veto right now or something like that under this President or maybe the last one.

I kind of sense you're maybe more satisfied with leadership over there right now, too, which is OK with me, I think he's making a formidable effort.

Ms. **White**. I think HUD could be an adequate funnel to the fair housing groups, who would in fact do the testing.

Senator **Dixon**. Well we're going to pursue that in a minute.

Mr. Bradford, we haven't been fair to you to get your point of view before we get back and go over this testing business and so forth. Go ahead.

STATEMENT OF CALVIN BRADFORD, REPRESENTING THE CHICAGO FAIR HOUSING ALLIANCE

Mr. **Bradford**. Thank you, Mr. Chairman.

I think one of the things we have to recognize is that we have a dual housing finance market in this country. We have one market for whites and one is for blacks. We have a market where conventional lenders serve white neighborhoods and, as the neighborhoods change racially, they disinvest in those neighborhoods. And then those minority and changing neighborhoods are inundated by a veritable onslaught of mortgage banking companies with FHA and VA loans.

And because the FHA and VA loans are poorly monitored and there's poor regulation at HUD, this results in huge levels of foreclosure, abandonment, and blight in these neighborhoods. Meanwhile, these mortgage companies make huge profits exploiting racial change.

I point this up because no community can survive without a constant flow of private capital and credit which comes through the depository institutions and their initial withdrawal precipitates this process of a dual market.

Any policy by the administration, the financial regulatory agencies, HUD, the VA or the Justice Department that does not affirmatively challenge this dual market contributes to a process of housing apartheid in the United States.

When the articles first came out in the Atlanta Constitution Journal, Senator Proxmire asked the reg agencies to respond. Three of the four reg agencies responded specifically that one of the ways to explain away the poor lending records of depository institutions was that there were high levels of lending by mortgage bankers and FHA lenders.

Last October, John LaWare said essentially the same thing before you and this committee and came in again today and said it all over again.

It seems to me what they are saying is we have separate but allegedly equal markets. We reject the notion of separate but equal in South Africa. We reject it as a matter of Federal law in the United States. There is no reason to accept it in the mortgage markets.

The one option that the lenders present is that there are more home improvement loans sometimes in minority neighborhoods than in white neighborhoods. It strikes me this is really a form of blaming the victim. When you look at the fact that we force minorities to live in neighborhoods which typically have older housing (often housing distressed at 10 to 20 times the rates of housing in white neighborhoods). To say that a few lenders finally responded by making home improvement loans is not a sign of fair lending. I have submitted some additional comments on that.

I think it's important to note issues about affirmative requirements and about the effects tests again. As Constance Dunham Ford points out in the Boston study, and I quote:

> Even if the disparities in the mortgage market activity were not the fault of the lenders, banks and thrifts would be expected to help correct the situation.

The regulatory agencies are doing nothing to insure that lenders take affirmative steps to try and correct it, and I think that relates to this whole issue we've had about the affordability of lending for minorities.

I have looked at almost a hundred reinvestment agreements created by community groups because the regulating agencies wouldn't do their job. These lenders make loans to a full range of minority areas. They've invested in Chicago over $100 million predominantly in minority neighborhoods, to some of the poorest neighborhoods in the city and to some middle class minority neighborhoods. They have almost no defaults; I think there's only one less default out of 510 loans.

I've seen all over the country that private lenders can create mortgage products to serve any market they want, but they don't want to serve these markets and the regulatory agencies don't encourage them to serve these markets.

In the area of the effects tests, we know lenders do not hurl racial epithets at minority applicants and tear up their applications. They discriminate through a range of underwriting procedures that have been described here and also through processes as simple as not marketing in a neighborhood, having different hours than other branches or taking the branches they have in your neighborhood out of your neighborhood.

It seems to me that the lowest mark of the lack of applying the effects test comes from the application that actually started the Atlanta Constitution studies, an application by SunTrust. It was challenged on the grounds that they had developed only one mortgage product that was clearly not attractive to minorities and that they'd closed branches in minority neighborhoods.

The bank responded to the Fed that the effects test should not be applied to their chosen policies and practices, and the Fed responded by granting their application, with no conditions.

In 1989, another challenge was filed. After the challenge, John LaWare again came to your committee and told you there was no evidence of discrimination. The challenge again claimed that they had closed more branches in minority neighborhoods, in some neighborhoods where their local deposits had actually increased, and again the Fed approved the application. And John LaWare comes today and tells you he can't find any discrimination. I think these are the activities of the regulatory agencies that show that they don't have a commitment.

I was sitting in front of the special assistant for fair lending from the FDIC and I think when you interview Ron Wienk, you'll want to go interview Pat McCormick as well and find out how much she does or does not get involved in any of the activities at the FDIC.

The lenders have continued to allow massive forms of disinvestment. In Illinois, for example, in your own State, there are over 320,000 people in the near south suburbs of Chicago in areas that are racially changing or that are racially diverse. They are having serious problems with the inundation of FHA and VA blight in those neighborhoods; they need conventional loans.

Calumet Federal Savings and Loan is one of the largest institutions that allegedly serves that area. It makes 99.8 percent of its loans outside of those minority neighborhoods, 90 percent of them in Colorado. This seems to be perfectly acceptable to the Office of Thrift Supervision.

And finally, I would like to say that there are institutions that have an outstanding record in serving minority loan needs who are not only not recognized by the reg agencies but seem to be punished for doing it.

In 1989, the Federal Reserve, which turns down almost no CRA applications, turned down an application from Continental Bank allegedly on CRA grounds. And in 1990, they forced Harris Bank in Chicago to withdraw an application allegedly on CRA grounds. Continental Bank and Harris Bank have two of the most outstanding records of special programs serving minority neighborhoods, not only in the State of Illinois but in the United States, particularly for large banks.

Talman Federal Savings and Loan has led the way for over a decade in serving minority neighborhoods in Chicago when no one else would do it. They are responsible, in some cases singlehandedly, for saving communities from being predominantly Government loan communities.

But because the Office of Thrift Supervision will not allow them more time to meet their capital reserve requirements for FIRREA, they will have to sell their institution to outside investors who do not share that commitment. And the leadership of this commitment will be lost.

These are decisions that could have been made otherwise by the regulatory agencies that seem, in effect, to punish institutions with outstanding records while they continue to grant applications to institutions like SunTrust, whose records are constantly challenged, and in the cases like SunTrust where the bank literally admits that it has policies that are discriminatory in effect.

I have submitted several sets of recommendations from the Chicago Area Fair Housing Alliance. They include problems with HUD as well as problems with the regulators. I would just highlight a couple of the recommendations that I don't think have been covered before.

The Fair Housing Act, we think should be amended to establish clearly that actions that have a discriminatory effect, whether or not intent is proven, are violations of the act. In other words, make the act itself include the effects tests so there's no question in the courts and so that the slippery slope of Wards Cove does not come into housing.

And these provisions should also be included in the Community Reinvestment Act regulations.

The Fair Housing Act should be amended to extend the present affirmative requirements not only to regulatory agencies, but to all institutions they regulate that receive federal benefits or deal with Federal agencies.

Disclosure, as I think Allen Fishbein was mentioning, should be extended to insure not only that it covers all mortgage lenders, but that the public gets access to the loan logs. After all, it's been the public that's done all of the regulation and the enforcement; it's not fair now that you have passed a law to create more disclosure for the regulatory agencies to take it away.

HUD should set standards for evaluating fair lending and agree with the regulatory agencies that screening processes for fair lending will be done not only in examining institutions but every time there's a CRA challenge.

An important piece of legislation first drafted by National Peoples Action in a proposal that I have included is that institutions that violate the fair housing laws should not be protected by the favor of Federal deposit insurance which they receive from the Government. All of us now know out of our own pockets what a high cost we pay when institutions have to use that insurance, and it's a great privilege from the Government.

They propose a law that would essentially say that if you're found in violation of Fair Housing, and Equal Credit Opportunity, or Community Reinvestment Acts—not only by the reg agencies but in court—that those institutions could be sanctioned, up to and including removing deposit insurance. We think you'll find some rapid compliance if you get those kinds of penalties.

We do recommend that HUD and the agencies consult with the public and hold conferences and meetings to get public input by people who do understand fair housing before they implement their regulations.

And finally, that a special committee be set up, a review board, not only of the kind you've mentioned—and I can make some comments about how effective they've been—but an independent review board that can report to Congress on the Fair Housing and Community Reinvestment Act enforcement of these agencies.

Thank you.

[The complete prepared statement of Calvin Bradford follows:]

STATEMENT OF CALVIN BRADFORD

On Behalf of the Chicago Area Fair Housing Alliance, Et Al.

(See Signatory Page)

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

OF THE

SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

OVERSIGHT HEARING ON MORTGAGE DISCRIMINATION

MAY 16, 1990

Housing Finance and Race: A Time to End The Dual Market
Executive Summary

This country has a racially discriminatory, dual housing market that is supported and maintained by a dual housing finance system. Depository institutions, using conventional lending, disinvest in communities as they change racially - and continue to withhold credit to minority communities. This dual lending market is an essential component of the dual housing market.

As conventional lenders withdraw, an army of mortgage companies equipped with a seemingly endless and unregulated flow of FHA and VA supported loans moves into the void and creates a blaze of sales. Whites flee to the areas financed by conventional lenders and minorities are steered into each changing neighborhood with the promise of FHA and VA loans. The exploitation of racial fears to encourage white flight and reap the profits from a huge volume of sales and loans becomes a wildfire continually spreading through the healthy communities in its path. Lax regulation, poor monitoring and bad property management policies by HUD allow the infusion of government lending to result in high rates of foreclosure and abandonment. Thus, the firestorm of FHA/VA lending leaves behind a scorched earth of abandonment and blight. Once blighted, neither FHA nor conventional lenders will serve the communities.

In spite of the best intentions and legislative efforts of Congress, the policies and practices of the agencies insuring and regulating depository institutions - and of HUD, the VA, and the Justice Department - have actually encouraged the disinvestment and redlining of inner-city and minority communities and encouraged speculative investment. Congress and the Administration must be called upon again to insure that the laws for fair housing and fair lending do not get implemented by federal agencies in such a way that they become regulatory apartheid.

Any policy by the Administration, the financial regulatory agencies, HUD, the VA, or the Justice Department that does not affirmatively challenge this dual market in all its manifestations - or allows any branch of government to accept the position that separate housing markets are somehow equal - contributes to housing apartheid in the United States. History has shown us that policies that deal only with the conventional or government markets in isolation can actually make the impacts of the dual market worse.

The time has come to expose the structure of the dual housing finance market and mount a direct attack. This requires commitment on the parts of the financial regulatory agencies, HUD, the VA, the Justice Department, the Administration and Congress. There is a new spirit in the communities. In the past, fair housing groups tended to concentrate their efforts in white communities where minorities had no access. Community-based action groups and development organizations, as well as reinvestment groups, concentrated on the problems of rebuilding inner-city communities destroyed or weakened by disinvestment and exploitation. But as many of the once white communities subject to fair housing efforts have become the changing communities subject to exploitation and blight in the FHA markets, these two constituencies have begun to work together on the common problems of fair lending. What is the value of access if the profiteers in resegregation turn it into an opportunity for resegregation and blight? The problem must be solved at both ends by focusing on the common problems of discrimination and exploitation through the dual housing finance markets.

No community can achieve stability and economic health if it is not supported primarily by the private sources of credit and capital. The government markets can provide critical resources, leverage private funds, provide leadership in revitalization, and assume some extra risks - but they should never be allowed to replace the private financial markets. Now is the time for the government to join forces with citizens and act against the dual housing finance market in a single, unified approach involving both government and conventional lenders.

We recommend a full recognition of the existence and consequences of the dual housing finance market by all agencies involved in housing and a full reporting on the impacts of this market and the remedies being taken to eradicate this market in the HUD Secretary's annual report to Congress on discrimination in housing. We further recommend a range of actions, legislative, regulatory, and administrative to eliminate this dual housing finance market.

These recommendations include:

A. **The Effects Test**

1. The Fair Housing Act should be amended to establish clearly that actions that have a discriminatory effect, whether or not intent to discriminate is proven, are violations of the Act-- the effects test.
2. The regulations for the Community Reinvestment Act should be amended (as well as all guidelines for use of the CRA) to specifically include the effects test when considering compliance with fair housing laws.
3. HUD should revise its existing Fair Housing Regulations to specifically include the effects test and to indicate that this test will be applied to all institutions involved in the housing industry, including developers, builders, lenders, mortgage and hazard insurance providers, brokers, real estate agents, and members of the secondary mortgage markets.

B. **Affirmative Obligations**

1. The Fair Housing Act should be amended to extend the present affirmative requirements from HUD and the executive agencies to all lenders using government programs (including all HUD programs, VA, Farmer's Home Administration, all regulated financial institutions, and all lenders using the services of the Federal National Mortgage Association, the Government National Mortgage Association, the Federal Home Loan Mortgage Corporation, or any lender using loan funds generated in whole or in part by tax exempt bonding authority).
2. The regulations for the Community Reinvestment Act should be amended (as well as all guidelines for use of the CRA) to specifically extend the affirmative obligations of the act to fair housing activities and evaluations.

C. Disclosure

1. The disclosure provisions of the Home Mortgage Disclosure Act should be amended to specifically include all mortgage banking and all mortgage broker transactions for lenders making more than five loans in any metropolitan area, regardless of their asset size.

2. The public disclosure provisions should include disclosure - in hard copy - of the loan log data by the lending institution at the time the data are transmitted to the regulatory agencies on March 1 of each year. These logs should be ordered by census tract location, and within that they could delete the date of each application and the lender's loan code number.

3. HUD should disclose in hard copy, quarterly, by lender, and by census tract for each lender, the number of loans in foreclosure and the origination dates of these loans. Foreclosure data are already reported to HUD by its lenders. This will allow both HUD and the public to monitor lenders with high foreclosure rates in specific communities - especially those with foreclosures so early in the term that they indicate poor underwriting.

D. Monitoring and Reporting

1. The federal regulatory agencies should include in annual reports to Congress on fair housing the results of an analysis of the dual housing finance market in each metropolitan area, along with indications of the lenders whose individual patterns place them at the lowest levels of meeting fair housing goals.

2. HUD should establish a set of public standards for an analysis of lending patterns based on the HMDA data on applications, race, sex and income. It should request the regulatory agencies to screen individual lenders by these standards when they are examined, when a protest is filed under the CRA, or when a fair housing complaint is filed against a regulated depository institution. HUD should conduct its own analysis for all lenders reporting to HUD. An investigation should be initiated against all lenders failing to pass this initial screen.

3. The Secretary of HUD should include a special section on the dual housing market in his report to Congress on fair housing. This should include all efforts to monitor and intervene in the dual housing market and a review of all actions taken to identify discrimination and take action under the Fair Housing Act.

4. HUD should also include in its Fair Housing report to Congress all efforts to coordinate its own offices, programs, and activities to insure that fair housing opportunities are not lost or impaired through lack of coordination or cooperation in the various HUD offices and programs.

E. Enforcement

1. Institutions that violate the fair housing laws should not be protected and favored by federal deposit insurance. Amend the banking acts to require sanctions, up to and including the elimination of deposit insurance and liquidation of assets, for institutions that are found to be in violation of the Fair Housing Act, the Equal Credit Opportunity Act, and the Community Reinvestment Act. Such a concept is contained in legislation proposed by the National Peoples Action (as the "Financial Institutions Fair Practices Accountability Act", described in a circular from the National Training and Information Center).

2. HUD should be required to suspend from FHA programs lenders that violate the Fair Housing Act or the Equal Credit Opportunity Act. In applying this standard for review, HUD should employ the standard for exploitation of discrimination in the market established in the case of Clarke v. Universal Builders. This would impose sanctions against the exploitation that presently masquerades as affirmative action. Considerations for sanctions should include high early foreclosure rates and abuses of the direct endorsement privilege, especially in minority and transitional communities.

3. HUD should act to enforce the prohibition against minimum loan amounts for FHA loans so that lower-income communities have access to FHA lending.

F. Housing Programs and Policies

1. Congress should not pass legislation providing for additional concentrations of FHA lending in minority communities - but should pass legislation against the restriction of any type of credit in minority and lower-income communities as a violation of the law.

2. HUD should modify its FHA programs to remove prepayment of insurance and restrictions on a seller providing any part of the closing costs so that these costs are not folded into loan amounts, resulting in loan to value ratios of over 97%.

3. HUD should affirmatively market the Mortgage Assignment Program and make every effort to use the program to give as many homeowners as possible a chance to keep their homes after they have gone into default.

4. HUD should make every effort to provide homes in its inventory at the lowest possible prices at the earliest possible time to community-based development organizations that have the capacity to repair the homes and place them back on the market at affordable prices.

5. HUD should require that recipients of Community Development Block Grant funds conduct a study of barriers to fair housing, including lending discrimination, and propose affirmative fair housing actions, as a condition for

fair housing certification to receive CDBG funds. Presently this is only provided as an option that is seldom used.

G. Counseling

1. HUD should request and Congress should grant a substantial increase in funds for pre-purchase, fair housing, and default and delinquency counseling by community-based organizations as the most efficient and sound means of reducing losses and preventing abandonment and blight.
2. HUD and the VA should target pre-purchase and fair housing counseling to specific high risk situations, such as communities with high concentrations of FHA/VA loans, first time homebuyers and homebuyers with low-incomes and/or minimum downpayments, and should require pre-purchase counseling prior to the time a prospective buyer enters the market to seek housing.
3. The regulatory agencies should specifically define counseling as an activity that aids reinvestment and is considered when reviewing the activities of institutions under the CRA, the Fair Housing Act, and the Equal Credit Opportunity Act.

H. Technical Assistance and Research

1. HUD should reverse its present policy on the national testing it undertakes and allow the data to be used in court actions and for research and analysis by the fair housing groups who carry out the testing for HUD. The most extensive evidence of discrimination in sales and rental - and possibly similar data on lending in the future - is hidden from view and use under the present policy.
2. HUD, the regulatory agencies, and the VA should provide guidebooks and other materials to assist local governments, state and local agencies, and the public in using HMDA and other forms of data useful in analyzing local housing markets and identifying possible signs of discrimination.
3. The regulatory agencies, HUD, and the VA should consult with the public groups, organizations, researchers, and agencies that have experience in identifying lending discrimination before they develop disclosure and examination regulations and standards.
4. The regulatory agencies, HUD, and the VA should hire consultants or staff people with expertise in lending discrimination and not rely on economists, program administrators, or examiners to provide them with their expertise and understanding of these issues.

I. Hearings and Reviews

1. Recent history has shown that Congressional hearings evoke the most noticeable responses from the regulatory agencies. Fair Housing and Community Reinvestment Act oversight hearings should be used forcefully to induce reform, as has been done so well in the past.

2. Citizen review boards are a powerful tool for accountability. An independent review board should be established to review and report to Congress on the fair housing and community reinvestment efforts of the federal financial regulatory agencies, HUD and the VA.

END of EXECUTIVE SUMMARY

Housing Finance and Race: A Time to End The Dual Market

by Calvin Bradford
Community Reinvestment Associates

The time has come to deal with the financial forces that drive the racially discriminatory, dual housing market. For years we have attacked the patterns of segregated housing and segregated communities based on the practices of sales and rental agents, racial steering, and the overt denial of opportunities to minorities in white communities. But credit is the life blood of the real estate industry.

Research shows that there is no relationship between mortgage risk and race and that there is no relationship between race and housing values or blight. But, there is a relationship between the disinvestment of the dual housing finance market and neighborhood decline. While progress has been made legislatively and in the courts in dealing with discrimination at the level of the real estate sales and rental transactions, very little has been done to deal with the dual housing finance market that drives the real estate sales and development industries.

Indeed, many of the gains made in the last two decades have been reversed by the policies of the Federal agencies that regulate depository institutions (The Federal Reserve Board [Fed], the Comptroller of the Currency [COC], the Federal Deposit Insurance Corporation [FDIC], and the Office of Thrift Supervision [OTS - previously the Federal Home Loan Bank Board, or FHLBB). In spite of the best intentions and legislative efforts of Congress, the policies and practices of these agencies - and of HUD, the VA, and the Justice Department - have actually encouraged the disinvestment and redlining of inner-city and minority communities and encouraged speculative investments in white areas. Congress and the Administration must be called upon again to insure that the laws for fair housing do not get implemented by federal agencies in such a way as to create regulatory apartheid.

One of the casualties of deregulation, along with the monumental costs of the savings and loan debacle, has been the enforcement of fair housing and equal credit opportunity laws. Lenders have been allowed to continue to allocate their resources toward the building and maintenance of white communities while withholding their credit from minority communities and transitional communities. Lacking access to conventional lending, minority and transitional communities are left to be served by the federally insured and guaranteed markets of the FHA and VA lending programs.

Properly regulated and carefully prescribed, HUD's FHA programs are a powerful drug for housing ills. But unregulated and over prescribed, they are extremely toxic and lethal to entire communities. HUD has acted more like a drug dealer than a doctor. The abuse of these programs, combined with lax regulation by HUD and the VA, and the innate higher risk of these government loans in their own right, condemns these minority and transitional neighborhoods to a future of abandonment and blight.

The public is paying a huge price for the excesses of the S&L industry and the poor record of regulation. But people in minority and transitional communities have already paid for that three times. They paid when these institutions disinvested in their communities. They paid when FHA/VA was allowed to come in and devastate their communities. They paid again with the costs of the bailout. Now they deserve to get something back. Yet the regulatory agencies charged with enforcement of the fair housing act have simply endorsed the dual market that has destroyed their communities.

The Community Reinvestment Act imposes an "affirmative" requirement on lenders to serve the needs of all the people and neighborhoods in the communities they serve. The Fair Housing Act requires that they not discriminate. Thus far, case law has maintained the position that policies that discriminate in effect violate the law. Taken together, this imposes an affirmative requirement on lenders to serve the needs of minority communities and to insure that no policies, direct or in effect, fail to take full advantage of opportunities to serve minorities. But these agencies have not only failed to apply an affirmative standard, they have blessed the dual market, defended the dual market, and actually aided and abetted in the wholesale disinvestment of minority communities by the institutions they regulate. The effect has been documented in scores of studies of lending patterns in almost every major metropolitan area of the country. The most notable recent study is the Pulitzer prize winning investigation by Bill Dedman of the *Atlanta Journal and Constitution* ("The Color of Money", 1988).

In responding to these studies, the regulatory agencies invariably declare that these studies ignore the government supported FHA/VA market and the lending of mortgage bankers and mortgage brokers - who originate three-fourths of all these government loans. Indeed, last October, in hearings before the Senate Subcommittee on Consumer and Regulatory Affairs, John LaWare, of the Board of Governors of the Federal Reserve System, responded to precisely these studies and commented that these patterns could be explained by factors other than discrimination, such as the "traditionally high level of activity by mortgage bankers and finance companies..."

Such responses are terrifyingly similar to the case once made against integrating lunch counters and schools. The argument is that we have separate - but allegedly equal - institutions for minorities. As a matter of international policy, we reject this argument in South Africa. National law has struck down the lunch counter argument not only for eating, but for all forms of retail trade. And just as the separate school system was not equal, so the separate institutionalization of a single market of government loans for minorities as opposed to a widely diverse and heavily competitive mortgage market for whites is not equal.

This market is separated on racial lines. It is separated between private depository institutions (conventional lenders) and government insured and guaranteed FHA and VA lending through mortgage companies. This market of government domination in minority and transitional communities is not only unequal, but it results in massive destruction to the markets where it is concentrated in older, existing cities. It results in high concentrations of abandonment and foreclosure. But it is so lucrative to the real estate agents and lenders involved that it can drive out the conventional lenders even when they want to reinvest. Finally, the specter of this government market is so terrifying that its introduction into a new community can destroy a once healthy market and eliminate the chance for racial and social integration to succeed.

This segregated market of neighborhood destruction contributes to the false belief that racial change undermines a healthy community. Fear of racial change, often supported by conventional lenders disinvesting as racial transition is anticipated, creates an incentive for reaping huge profits from the process of rapid racial resegregation. Real estate agents, using racial steering and subtle forms of panic peddling, are the first agents of transition. As conventional lenders withdraw, or as they cease to market their products, an army of mortgage companies equipped with a seemingly endless and unregulated flow of FHA and VA supported loans moves into the void and creates a blaze of sales. Whites flee to the areas financed by conventional lenders and minorities are steered into each changing neighborhood with the promise of FHA and VA loans. The exploitation of racial fears to encourage white flight and reap the profits from a huge volume of sales and loans becomes a wildfire continually spreading through the healthy communities in its path.

Without the strength and stability of conventional lenders in these communities, mortgage bankers and brokers, working with a cadre of real estate agents, reap profits from massive and rapid racial resegregation. Lax monitoring and bad property management practices by HUD and the VA have resulted in high levels of abuse - leading to extensive abandonment and blight in the communities undergoing change. Unwary home buyers are often sold defective homes or homes they cannot afford - and the firestorm of FHA/VA lending leaves behind a scorched earth of abandonment and blight.

This process so undermines the stability of the community that the appraisal consultant to the U. S. League of Savings Associations once wrote a series of articles in its journal suggesting that lenders measure the levels of FHA lending and withdraw from communities with high volumes of these loans. Thus, the initial discrimination and disinvestment of minority and transitional communities by depository institutions leads to a self-fulfilling prophecy of decline later used as a defense against fair housing and reinvestment.

Any policy by the Administration, the financial regulatory agencies, HUD, the VA, or the Justice Department that does not challenge this dual market - or allows any branch of government to accept the position that separate is equal - contributes to housing apartheid in the United States. History has shown us that policies that deal only with the conventional or government markets and not the entire market can actually make the impacts of the dual market worse. Ultimately this is not just bad civil rights policy, it is bad economic policy as well. The devastation caused by the racial resegregation syndrome and the massive amounts of federal dollars that are needed to rebuild the communities left in its path will come home to haunt all those who turn their backs on the problem today.

Community groups, civil rights organizations, and fair housing groups have had to carry the burden of CRA and fair housing enforcement in the absence of responsible intervention by the financial regulatory agencies. These groups have fashioned more than 100 different commitments and agreements with lenders across the country. These programs have demonstrated that there is no need or market that cannot be served by creative and affirmative efforts of lenders in partnership with local community groups, programs, and government agencies. There is no market need that is served by FHA or VA that cannot be served by some kind of private lending program - with lower losses and without a destructive effect on the community.

The Discrimination Embedded in the Home Sale Markets

A. Appraisers and Appraisal Values in the Industry

Racial discrimination and false beliefs about lending risks and property value declines related to racial change are embedded in the very principles of real estate appraisal and underwriting that guide traditional lenders in their decisions. Homer Hoyt, one of the founding fathers of real estate principles and theory, included in a 1933 text a list of ethnic groups ranked form those alleged to have the most positive influence on values to those with the most detrimental influence. English and Germans were at the top of the list and "Negroes" and "Mexicans" were at the bottom of the list given to him by a real estate agent from the West Side of Chicago.

(*One Hundred Years of Land Values in Chicago*. Chicago: University of Chicago Press, page 316).

In 1932, another of the fathers of real estate principles and theory, Frederick Babcock, wrote this about ethnic change and decline:

"Most of the variations and differences between people are slight and value declines are, as a result, gradual. But there is one difference in people, namely race, which can result in very rapid decline. Usually such declines can be partially avoided by segregation and this devise has always been in common usage in the South where white and negro populations have been separated." (*The Valuation of Real Estate*. New York: McGraw-Hill, 1932, page 91)

These beliefs were incorporated into the professional values, ethics and teachings of the National Association of Real Estate Boards (now the National Association of Realtors) and the professional appraisal organizations. These views on race and property value were incorporated into the early texts of the American Institute of Real Estate Appraisers in 1935. Even Hoyt's list was incorporated in real estate appraisal manuals that were in print in the 1960s. Homer Hoyt himself was hired by the FHA to develop its underwriting standards in the 1930s. FHA recognized restrictive covenants until the practice was prohibited by President Eisenhower. Until the 1960s, and the aftermath of the urban riots, FHA was so restrictive in its own lending that the term redlining was coined to describe the inner-city and minority areas defined on FHA maps as places where it would not lend.

B. Real Estate Agents, Lenders and Mortgage Investors

Real estate agents make their money from commissions on homes sold. Without financing there is no sale. So agents are dependent upon the values and willingness of lenders to finance homes in the areas the agent serves. When homes are listed, they are appraised by the agents, incorporating the values of appraisal into the early stages of the marketing process.

Federal law requires that real estate loans made by insured institutions be based on values determined by professional appraisers. Since lenders are concerned that the value of a property not fall below the balance of a loan over its entire life, they are especially sensitive to appraisal principles that predict value trends. Beliefs that racial change leads to falling property values are translated by the actors in the single-family market into redlining and disinvestment for minority communities and communities with racial diversity. Over time, the mere characteristics of communities where minorities were forced to live - older areas with diverse land uses and housing types - also became standards for loan denials.

Typically, regulated lenders will not make loans at amounts higher than 80% of value unless they are insured against losses. FHA and VA loans provide the most complete insurance, with FHA insuring the entire value of the loan and the VA guaranteeing the full value. Private mortgage insurance on conventional loans protects the lender from the portion of the loan above the 80% of value limit. But the full insurance by FHA, and the certainty that FHA will take the property from the lender after foreclosure and pay the claim, encourages lax underwriting and abuse - providing the realtor, the lender, and the purchaser of the loan with virtually no risk of loss regardless of the fate of the loan. Only the homeowner, the local community and the government bear the burden of the loss.

Members of the secondary mortgage market and those institutions that insure mortgages and make them salable in the secondary markets also use professional appraisal standards and principles to develop their underwriting standards for loans they are willing to purchase. Here, again, the discrimination in appraisal practices and principles has created many standards that are discriminatory in effect - if not overtly discriminatory in intent. Today, all lenders want to know that the loans they originate can be sold in the secondary market. This creates liquidity and protects the lender against holding a portfolio of loans that are unprofitable.

The values of the secondary market are most important for mortgage companies. Mortgage companies - mortgage bankers and mortgage brokers - do not have deposits, though many of these companies are owned by corporations that also own banks and savings institutions. Mortgage bankers borrow on commercial lines of credit to originate loans that they sell to the secondary market. Mortgage bankers make money in originating the loans and in servicing the loans for the investors who purchase them. Mortgage brokers originate the loans, sometimes acting as direct agents of the investors, but do not service the loans. These mortgage companies are most dependent upon the opportunities and limitations of the secondary markets, since they must sell their loans.

Real estate agents are often the initiators of racial transition, but they reflect the opportunities and limitations placed upon them by lenders. Lenders, in turn not only reflect their own standards, but those who insure and invest in the mortgages they originate. Thus, the capital and credit markets, and their views of racial change, and the practices of the real estate development and sales markets reinforce each other in ways that, in neighborhood after neighborhood, result in racial segregation and disinvestment.

The Dual Housing Finance Market

A. The Traditional Dual Housing Finance Market

As a result of the discrimination that has been incorporated into the very principles and values of the real estate markets, minorities and people in minority or transitional communities - or even near communities of racial transition - have suffered from discrimination in lending. Historically, both FHA and the conventional markets redlined against such communities. Minorities were forced to purchase houses with cash or resort to buying on contract. Real estate agents exploited this condition by buying properties from whites - often peddling the fear of racial change to get properties at bargain prices. Then these agents would sell the homes on installment contracts to minorities at inflated prices and high interest rates. Other developers built new homes and sold them to minorities on contract under the same conditions. When the buyer missed a single payment - which was common with the high prices and interest rates - the owner evicted the contract buyer and started the process again.

This process of exploiting the discrimination against minorities was limited by the need to find lenders willing to speculate on the properties purchased or built by the contract sellers. Some of the savings institutions that participated in this process over extended themselves in this speculation - resulting in a rash a failures in the middle and late 1960s. Finally, a class action suit in Chicago against contract sellers of both existing and new homes slowed this form of exploitation. In the case of Clarke v. Universal Builders, the court ruled that it was a violation of federal law to exploit the discrimination in the market and profit from it - even if you did not create the discrimination.

B. The Rapid Resegregation Syndrome

After the urban riots of the 1960s, discrimination in housing became a major concern in federal policy. This resulted in the passing of the Fair Housing Act of 1968. But in terms of actual federal policy toward lending discrimination, the government did not actively seek to reverse discrimination by conventional, depository institutions. Instead, it intervened by changing FHA (and consequently VA) policies radically.

FHA literally reversed its redlining practices and inundated minority and transitional communities with access to FHA lending. This did create access for minorities in the housing markets. But, it had three fatal flaws that eventually rendered this a policy of destruction of minority and racially diverse communities in a process of wholesale exploitation and rapid resegregation.

First, conventional lenders seldom used FHA lending. FHA, and VA lending was the specialty of mortgage bankers and brokers who made, and still make, about 75% of all such government loans. Mortgage companies specialized in these loans because the insurance and guarantees made them easily salable in the secondary markets. Thus, this government policy literally left the conventional lenders out of the process of fair housing and reinvestment. It relegated minority communities to a government housing finance market, while white communities were served by all sectors of the market.

Second, because these loans were completely insured, neither the mortgage companies that originated them nor the investor that purchased them - basically FNMA - cared about the soundness of the loans. To make matters worse, in August of 1968, the FHA Commissioner issued the infamous "Brownstein" memo, that ordered FHA offices to insure any property that did not immediately threaten the physical health of the inhabitants. This opened the flood gates to massive fraud, abuse and scandal in the underwriting of FHA loans.

Third, even without these abuses and scandals, the concentration of FHA lending in communities with lower incomes and older housing insured higher foreclosure rates among new and unwary home buyers. Until this time, FHA was used primarily for new construction and in newer areas. With its very low downpayments and liberal credit underwriting policies, it left many home buyers with few financial resources. In newer homes this was not a critical problem. In the initial years, all the systems of the home were new and did not need major repairs. Over time, the rapidly increasing property values provided new equity against which one could borrow for major expenses. One could always sell the home for enough to pay off the loan, if necessary.

But in older areas where the homes often needed major repairs soon after they were purchased, the liberal financing left homeowners without the resources to meet these needs. Property values did not rise rapidly in these areas and there was no new equity to borrow against. Without pre-purchase counseling, or default counseling after people got in trouble, thousands of people found themselves in foreclosure. This was compounded by the practices of the mortgage companies that filed for foreclosure as soon as possible to avoid servicing costs and to get the insurance proceeds.

The result was a more massive exploitation of racial change than ever imagined with contract sales. With the government taking all the losses and the communities suffering all the devastation, real estate agents teamed up with mortgage companies to reap huge profits from accelerating racial change through the new FHA/VA policies. The process of rapid racial resegregation through the dual housing finance market was first identified by the anti-redlining movement of the 1970s, led by the National Peoples Action. It was defined in the report of the

National Commission on Neighborhoods in 1978. The first empirical study using both individual FHA and VA data was done by Calvin Bradford in a study done for the plaintiffs in a suit against the Veterans Administration (Jorman, et al. v. the Veterans Administration, et al.) in 1984. This study identifies four components of the disinvestment-resegregation syndrome:

1. An initial withdrawal by depository institutions and a change to a mortgage lending market dominated by mortgage companies;
2. An extreme concentration of FHA/VA lending in racially changing neighborhoods;
3. Unusual and sudden rapid increases in the rates of home sales in these communities; and
4. Close relationships between a small number of real estate agents and mortgage companies doing a high volume of activity with each other.

As an added benefit, mortgage companies joined with banks and savings institutions in financing the development of new - white communities - financed through FHA, VA, and the full range of conventional loans. In places like Chicago, this provided a ready haven for fleeing whites and a bonus for mortgage companies that could make money on both ends of the process of resegregation and white flight.

With no access to the stable forces of conventional finance, racially changing communities turned into a sea of abandonment and blight. At one point, HUD had over 100,000 homes in its inventory. As one author wrote, whole cities were "destroyed for cash." Indeed, cities like Detroit, Chicago, and Cleveland were so devastated by this resegregation process that they are still struggling to recover. Parts of these and many other cities have been reduced to wastelands - where millions of dollars of HUD Community Development Block Grant (CDBG) funds are now used trying to rebuild what FHA and lack of fair housing enforcement destroyed.

C. The Effects of Banking Policies

While it is pervasive discrimination that fuels the dual housing and lending markets, the actual practices typically do not indicate intentional discrimination. Lenders do not hurl racial epithets at minority applicants and tear up their loan applications. The process is implemented through more subtly. Disinvestment typically takes place simply by not marketing lending products to real estate agents in minority or transitional communities. It takes place through policies of minimum loan amounts, higher points for smaller loans, restrictions on financing older homes, or restriction on financing properties in areas where there are mixed land uses or great diversity in the types of residential properties, etc.

All of these standards have been shown to have the effect of restricting loans in areas of minority concentrations or areas in racial transition. Sometimes, measures of the resegregation process itself are coded in neutral terms and used in underwriting loans. When the Justice Department forced the U.S. League of Savings Associations to remove the category for neighborhood change from its "Green Hornet" appraisal form, it was replaced with a space to record "velocity of sale", a clear code phrase for the rapid increase in sales that accompanies the resegregation syndrome.

Thus, the crux of fair housing enforcement against lending discrimination is the application of the effects test. The effects test establishes that acts that may be neutral on their face, but that have a discriminatory effect, are violations of the law. While it is not specifically defined in the Fair Housing Act, it has been supported by a broad body of case law. This case law provides the basis for the inclusion of the effects test in the regulations that implement the Equal Credit Opportunity Act. Any wavering from the use of the effects test by federal agencies and the courts undermines attempts to promote fair lending.

The Age of Reform

The 1970s saw an age of reform. This resulted from a massive neighborhood movement against redlining and active litigation and organizing for fair housing reform. The Home Mortgage Disclosure Act was passed in 1975 - making it possible for people to expose the redlining and disinvestment by conventional lenders. The Community Reinvestment Act was passed in 1977, creating an "affirmative" obligation on the part of banks and savings institutions to meet the credit needs of all the people in the communities they served. The Federal Home Loan Bank Board became the first regulatory agency to develop specific regulations against redlining and prohibit practices that were discriminatory in effect. The FHLBB even filed an *amicus* brief in a redlining case (*Laufman v. Oakley Building and Loan Company*), making clear its opposition to the practice.

Civil rights and fair housing groups stepped up their activity. A dozen of these organizations joined in a suit against the federal financial regulatory agencies for lack of enforcement of the Fair Housing Act (*Urban League, e[illegible] v. The Comptroller of the Currency, et al.*). This forced three of the regulatory agen[illegible]o develop loan log registers to monitor discrimination in lending.

The Leadership Council for Metropolitan Open Communities, supported by the Business and Professional People for the Public Interest, filed suit against both the FHA and VA for allowing their programs to be used in resegregation in the Marquette Park area of Chicago. This led to the creation of the only mandatory pre-purchase counseling program in the nation. A program that created access for minorities to the entire housing market and, at the same time, provided potential home buyers with the knowledge and skills to deal with the financial problems of home ownership. Community organizations in this community credit the initial use of the program with reducing the foreclosure and abandonment problem to a minimum and protecting the economic future of this racially, culturally and economically diverse community of Chicago Lawn.

Suits by community organizations and the Department of Justice cleaned up some of the FHA abuses. Scores of mortgage lenders, real estate agents, and FHA employees were convicted of crimes. A suit filed against HUD in Chicago led to the creation of the Mortgage Assignment Program designed to offer homeowners an additional chance to avoid foreclosure after the mortgage company has filed against them. It has saved thousands of people from foreclosure. By 1981 the huge HUD inventories of foreclosed properties had been reduced to about 19,000, a reduction of over 80,000 from the 1970s.

Pressure from community organizations and the Senate Banking Committee forced FNMA and Freddie Mac to revise their underwriting and service manuals to prohibit standards that were discriminatory in effect and to provide examples of such practices to the lenders from whom they bought loans.

Finally, the Department of Justice filed suit against the major professional real estate appraisal organizations, the Mortgage Bankers Association and the professional association of savings institutions charging discrimination in their practices, teaching materials, publications, and even codes of ethics. As a result major changes were made in the materials used by these organizations.

Deregulation and the Reinforcement of the Dual Market

But with the deregulation of the 1980s we see a rejuvenation of the dual housing finance market and the rapid racial resegregation syndrome. In the spirit of deregulation, the federal financial regulatory agencies reduced their fair housing and CRA compliance efforts. CRA enforcement was virtually left to community groups. When regulators failed to intervene on their own - as prescribed by the law - they literally blamed community groups for not forcing them to do their jobs. In the July, 1989, CRA hearings before the Senate Banking Committee's Subcommittee on Consumer and Regulatory Affairs, the Federal Reserve Board responded to a question about how often it had granted applications to institutions with poor CRA records by stating that "...the Board approved about 70 applications where the CRA rating was less than satisfactory -- and very few of these involved CRA protests."

Two of the three regulatory agencies that had developed loan log registers discontinued them as soon as the settlement decree expired. The third agency, the FHLBB, failed to use the data from its logs in examinations. When the summary data from these logs was secured by the *Atlanta Journal and Constitution* through a Freedom of Information Act request, the data revealed huge differences between white and minority rejection rates in metropolitan areas all across the country.

For their part, FNMA and Freddie Mac had deleted almost all of the anti-redlining language and examples from their underwriting and service manuals. Only concerted efforts on the part of national coalitions of community organizations, led by the National Peoples Action, has forced FNMA to re-introduce most of the original language.

For HUD's part, the monitoring of FHA lenders has become so limited that abuses are reappearing. Once again, people are buying some homes with code violations and in need of major repairs. As a result some foreclosures are taking place in the first year of the loans - a clear sign of poor underwriting. The Direct Endorsement program that has worked so well as an efficiency move in processing loans in the overall FHA market provides an opportunity for those exploiting racial change to operate with minimal HUD supervision or review. The inventory of FHA homes has climbed in the 1980s to almost 96,000 properties in 1988. This is often brushed aside as a problem restricted to the economic problems of Denver, Oklahoma and Texas. But this increase reflects a general increase in minority and transitional communities where the process of racial resegregation is reasserting itself in the face of poor fair housing regulation of depository lenders and poor regulation and monitoring of FHA lenders by HUD.

HUD did not expand pre-purchase and default and delinquency counseling, which once provided security and stability to communities like Chicago Lawn. HUD has reduced its counseling activities, and virtually abandoned the counseling program in Marquette Park. Over $45 million in private investment in the residential and commercial redevelopment of that community is now threatened by the wave of foreclosures that have appeared in the wake of HUD's closing down the counseling program.

In the south suburbs of Chicago, a diverse and racially changing area of over 300,000 people, communities once devastated by FHA/VA practices of the past now have an additional 2,000 - 3,000 foreclosed and abandoned homes to cope with as they struggle to recover from initial blight. Meanwhile some of the major local financial institutions have disinvested. For example, Calumet Federal Savings and Loan invests 90% of its loan funds outside of this local service area - mostly in Colorado. For its 1988-1989 mortgage lending, it made just 0.2% (two tenths of one percent) of its loans in the nine minority and racially diverse suburbs in its service area (Harvey, Markham, Riverdale, Dixmoor, Robins, Hazel Crest, Country Club Hills, Sauk Village, and Chicago Heights - 33 census tracts with 9 loans totaling only $267,000). These patterns are reappearing in communities all across the country.

While the inundation of FHA/VA lending is a problem for minority and transitional communities with some moderate and middle incomes, FHA/VA lenders often impose minimum loan amounts and charge higher points for lower value mortgages - effectively redlining even FHA and VA from lower-income communities. The National Training and Information Center (NTIC) conducted a survey of the major FHA/VA lenders in several metropolitan areas in the summer of 1989 and found that most of these lenders charged higher points on lower mortgages and several impose minimum loan amounts on FHA loans, in spite of a direct provision in the Housing and Community Development Act of 1987 specifically prohibiting such a practice. HUD was given the results of this survey in August of 1989. NTIC has yet to receive a response.

Along with these problems, FHA has adopted practices of prepaying all insurance fees up front, and folding these and other closing costs into the mortgage - often producing mortgage amounts well over 100% of the value of the home. Low downpayment loans - especially without proper counseling - generally have higher loss rates - and loans well in excess of the home value provide an incentive to walk away from the property if the borrower gets in trouble - as there is no way to sell the home for enough to pay off the mortgage.

HUD was required by Congress to provide disclosure data on the locations of FHA lending, but it has failed to produce any such data for the past eight years. In the years since the creation of the Assignment Program, HUD has been dragged into court several times for violating the provisions of the settlement that created the program and for trying to replace the program with one that provides less protection to FHA home buyers. Such disclosure supplies the major missing piece in mortgage lending studies that now rely on HMDA's disclosure of data for depository institutions, lenders that make few FHA or VA loans.

In Chicago where a state disclosure law provides disclosure for mortgage bankers, several studies by Anne Shlay, and the Woodstock Institute, show that in spite of the valiant efforts of a few savings and loans and the Neighborhood Lending Programs of three large commercial banks, minority and transitional communities still get fewer loans, and the loans they get are typically FHA or VA. Using a range of statistical techniques, Shlay's research shows that conventional lenders withdraw from communities as the rate of minorities increases and that mortgage companies inundate these communities with FHA/VA lending as they change. Studies in Philadelphia, Chicago, and other cities in the 1970s defined the resegregation syndrome at that time. Shlay's study shows that the resegregation patterns of the dual market are still present in the city of Chicago in the 1980s.

A forthcoming study by William Peterman and Qi Sanshi, of the University of Illinois at Chicago (funded by a grant from the MacArthur Foundation to the Chicago Fair Housing Alliance, using data originally collected by the Woodstock Institute), confirms that this process of conventional disinvestment and FHA/VA infusion accompanying resegregation occurs all across the Chicago metropolitan area, suburbs and city alike. The data indicate that the dual market even exists within financial institutions where a depository institution will cease lending as racial transition occurs, while its mortgage banking subsidiary infuses FHA/VA loans into the community.

Case studies for specific communities, like Chicago Lawn, detail patterns for individual lenders. Here, for example, conventional lending declined in the area of greatest racial change in 1987, while one mortgage lender alone, Margaretten, commanded 55% of the sudden infusion of government insured loans. Another study of mortgage lending and foreclosures in Chicago Lawn by the Woodstock Institute (for the year ending in September of 1989) indicated that Margaretten had 13% of the foreclosures in Chicago Lawn in this year, with an "average origination to default span" of only 17 months (*Mortgage Lending and Foreclosures in Chicago Lawn*. Chicago: The Woodstock Institute, 1990).

These are but some of the most complete and detailed of a host of sophisticated studies in Baltimore, Boston, Denver, Philadelphia, Washington, etc. Virtually all of these studies confirm the results of scores of other community, newspaper, and other reports that show significant differences in lending by race. But all this work has failed to impress the regulators. In 1983, Glenn Canner and Robert Avery, two economists for the Federal Reserve, conducted a statistical study of 100 metropolitan areas using HMDA and census data. Their limited and cursory data and techniques found only moderate lending differences by race. Yet, based on this limited study, using virtually no data about local housing markets or conditions, they concluded that there was very little redlining or discrimination nationally. They made this conclusion even though they admitted that it conflicted with many of the other sophisticated, and more detailed, local studies made of specific metropolitan areas - including some studies they had done themselves.

Since that time, the Federal Reserve has maintained its position that there is virtually no evidence of discrimination. Regulators try to ignore the studies of Shlay and others. Even in the face of Congressional inquiry and astonishment at the differences between lending rates and loan rejection rates for whites and minorities, the regulatory agencies remained passive. In responding to Senator Proxmire on the racial patterns revealed in the *Atlanta Journal and Constitution* articles, all the regulatory agencies filed reports in August of 1988. Three of these four agencies specifically pointed to the role of mortgage bankers and FHA/VA lending as an excuse for the patterns. The fourth agency, the FHLBB, admitted that its own loan log data revealed much higher rates of rejections for blacks than whites, but claimed that it was too busy with safety and soundness problems to do complete examinations and that the review it did make in Atlanta "does not suggest intentional discrimination" (August 19, 1988, letter from M. Danny Wall to Senator Proxmire, emphasis added).

Only the recent Boston study by Constance Dunham, et al., has momentarily slowed the regulatory agencies' aggressiveness in defending the dual market. She was, after all, an economist at the Federal Reserve in Boston - and her work supporting the earlier findings of a Boston study by Glenn Canner himself was published in a Federal Reserve journal. Moreover, as a former economist for a regulatory agency, her study notes that because of the affirmative obligations of lenders under the CRA "even if the disparities in the mortgage market activity were not the fault of lenders, banks and thrifts would be expected to help correct the situation" (K. Bradbury, K. Case, and C. Dunham, "Geographic Patterns of Mortgage Lending in Boston, 1982-1987," *New England Economic Review*. Federal Reserve Bank of Boston, September/October 1989, pages 3-30).

Now that Congress has amended the HMDA to require disclosure by all significant lenders and to require disclosure of data on the race, sex, and income of the buyer, along with data on applications and rejections, one would hope that the public would have more access to better data to track the dual market all across the nation. But the Fed's most recent proposal for public disclosure is to provide disclosure of the new loan logs only on computerized media to those with the technical resources to process and use such electronic media. They will not release to the public any data on race, sex or income by census tract. Staff at the Federal Reserve were to have met with community people with experience in lending discrimination before they devised the final tables for public disclosure, but no such meeting was held - and comments were solicited from only five people outside the regulatory agencies.

Since the critical intervention in the dual market is to identify the small areas on the edge of change and to compare lending in one neighborhood versus another, the omission of these data from public disclosure is a devastating blow to the community groups who have been the major enforcers of the CRA. To release these data only to those with the sophistication and economic resources to use computers is a form of discrimination in effect. Those who have used the past data the least - major research organizations and government agencies - will have access to all the data, while those who have used it the most - community groups - will find this form of disclosure useless. The regulatory agencies have failed to find patterns of discrimination - and now they seem to want to limit the public's ability to identify those patterns, in spite of the intent of Congress to do otherwise.

Finally, we are faced with the fact that while almost no applications are ever denied by the regulatory agencies on CRA or Fair Housing grounds, the Fed denied an application by Continental Bank in Chicago in 1989 and forced Harris Bank in Chicago to withdraw an application in 1990. Ironically, these measures were taken under claims of poor CRA performance. While it is conceivable that any lender might do more in fair housing, both of these banks are involved in several major community reinvestment and lending programs - programs that have been extremely effective at guiding conventional funds back into minority communities in Chicago for both single family and multi-family housing. Other lenders, all across the country, who have no record of affirmative programs for reinvestment and fair housing have routinely been granted applications - even in the face of continual challenges by community groups.

Talman Federal Savings and Loan has led the way for reinvestment in Chicago's minority communities. During the 1980's this sound and profitable institution aided the government by agreeing to acquire troubled institutions. Now the S&L bailout program is requiring Talman to raise equity for these acquisitions even though the government waived that requirement when Talman agreed to save the government from losses at the time of acquisition. By refusing to accept a Talman plan to extend the deadline for raising this equity capital, the Office of Thrift Supervision will force Talman to be sold to outside investors without the leadership in fair lending that has been the hallmark of Talman's past achievements. It appears from these actions that not only do the regulators endorse the dual housing market, but that they are willing to penalize those institutions that take aggressive steps to overcome conventional lending discrimination and act affirmatively on fair housing.

In the courts, the long-standing precedent of applying the effects test to legal cases is being eroded by some opinions. For example, the case that created the pre-purchase counseling in Chicago and released FHA from litigation was pursued through trial against the VA. The Seventh Circuit Court agreed with the District Court in that case (Jorman v. the Veterans Administration) that the VA was simply a victim of racism in the market and had no obligation to monitor the way its programs were used to fuel rapid resegregation. This was the ruling in spite of clear evidence that the VA was aware of the devastation resulting from the use of FHA lending in minority communities and had sent out directives warning its offices that the VA could be subject to the same abuses.

This is a far cry from the decision in Clarke defining the responsibilities of private companies not to exploit discrimination in the market even when they did not create it. The judge in the Jorman case continually complained that the plaintiffs had failed to show "intent". There is a real concern that the erosion of the effects test in the Wards Cove employment case looms as a trend for housing cases as well.

Probably the low mark of the retreat from applying the effects test in the regulatory arena is the 1987 application to the Fed by SunTrust, parent of Trust Company Banks in Atlanta, to buy another bank. A challenge by community groups pointed out that Trust Company had only one mortgage product and that it was not attractive to most minorities. The challenge also pointed out that the bank had closed several offices in communities after they became minority communities - even though the deposit base in at least one community increased significantly. The bank responded in a letter to the Fed that its attorney's did not think the effects test should be applied to their activities. The Fed granted the application with no response on the effects test question.

This challenge became the focus of one set of articles in the *Atlanta Journal and Constitution* series. In 1989, another challenge was filed against Trust Company, pointing out that it had continued to close branches in minority communities. In March of 1990 the Fed granted this application as well. When the Senate Subcommittee on Consumer and Regulatory Affairs held fair lending hearings in October of 1989, the representative of the Fed twice defended the overall fair housing record of his agency by indicating that it had found no "deliberate discrimination" in its reviews of lender behavior (pages 4-5 of the hearings).

A Time For New Initiatives

The time has come to expose the structure of the dual housing finance market and mount a direct attack. This requires commitment on the parts of the financial regulatory agencies, HUD, the VA, the Justice Department, the Administration and Congress. There is a new spirit in the communities. In the past, fair housing groups tended to concentrate their efforts in white communities where minorities had no access. Community-based action groups and development organizations, as well as reinvestment groups, concentrated on the problems of rebuilding inner-city communities destroyed or weakened by disinvestment and exploitation. But as many of the once white communities subject to fair housing efforts have become the changing communities subject to exploitation and blight in the FHA markets, these two constituencies have begun to work together on the common problems of fair lending. What is the value of access if the profiteers in resegregation turn it into an opportunity for resegregation and blight? The problem must be solved at both ends by focusing on the common problems of discrimination and exploitation through the dual housing finance markets.

No community can achieve stability and economic health if it is not supported primarily by the private sources of credit and capital. The government markets can provide critical resources, leverage private funds, provide leadership in revitalization, and assume some extra risks - but they should never be allowed to replace the private financial markets. Now is the time for the government to join forces with citizens and act against the dual housing finance market in a single, unified approach involving both government and conventional lenders.

SIGNATORIES (Partial)

NATIONAL ORGANIZATIONS:

National Peoples Action

CHICAGO AREA ORGANIZATIONS:

Business and Professional People for the Public Interest
Chicago Area Fair Housing Alliance
City of Country Club Hills
Fair Housing Coalition
Village of Glenwood
Greater Southwest Development Corporation
HOPE Fair Housing Center
Interfaith Housing Center of The Northern Suburbs
Leadership Council for Metropolitan Open Communities
Northwest Indiana Open Housing Center
Gary Orfield, Professor of Political Science
Village of Park Forest
William Peterman, Associate Professor of Urban Planning
South Suburban Housing Center
Southwest Community Congress
Village of University Park

OTHER ORGANIZATIONS:

Fair Housing Congress of Southern California
Fair Housing Council of Northern New Jersey
Fair Housing Contact Service, Ohio
Housing Opportunities Made Equal, Cincinnati, Ohio
Metropolitan Strategy Group, Ohio
Metropolitan Milwaukee Fair Housing Council

Issues in the Reporting of Home Improvement Loans
[Addendum to the Statement of Calvin Bradford]

Regulators are prone to point out that HMDA data sometimes show that while minority communities have lower levels of home mortgage loans, they have higher levels of home improvement loans. This is used to excuse low levels of home mortgage loans. The regulators fail to mention several major issues with these data. For example:

1. Reporting processes overestimate the levels of home improvement loans in minority communities and under represent the levels in white, affluent communities because-

    A. Almost all FHA Title I home improvements are reported by HMDA lenders, even though I have known since my term as President of the Evanston, Illinois, Housing Rehabilitation Board in 1975 that many lenders realize that the monies are often used for other things. Minorities have typically been forced to use these insured loans as the only means of gaining credit. For minorities who have to deal with discrimination in all types of lending, a home improvement loan is one of the few sources of credit available - and it is used for many other needs.

    B. As tax laws have shifted people towards using home equity lines of credit, these loans have been strongly marketed to affluent, and largely white, communities. Lenders do not report all of the home equity lines of credit that are common in middle-class and affluent communities - white communities - where the funds are often used for home improvement. Of course these funds are also used, like Title I funds, for all kinds of other needs as well. The results is that the major source of borrowing against equity for minorities almost always gets reported as home improvement lending while such borrowing in white communities frequently goes unreported.

2. The question is not do minorities get more home improvement loans, but do they get loans in proportion to the need and demand. Because minorities have been forced to live in older communities, they must buy homes that are more likely to need repairs and improvements. In addition, because their mobility is limited by discrimination in the markets, they are more likely to expand and improve the homes they have rather than buy a new home, as is more common in the white community. Thus, data on levels of home improvement lending that do not control for housing quality and mobility

are biased toward conclusions that minorities get fair access to credit, when the reasons for the higher borrowing levels may actually reflect discrimination in the markets.

3. Many local governments have established programs to rehabilitate and improve the older housing in their jurisdictions. These funds are typically marketed through conventional lenders, often through such programs as Neighborhood Housing Services. This happens in Detroit, Chicago, and many other cities. One program in Chicago operates on a $20 million reinvestment commitment from Continental Bank, a subsidized pool of $5 million from the Illinois Housing Development Authority, an operating grant from the City of Chicago, and on marketing done through the Chicago Neighborhood Housing Services program. It has made over 600 loans in less than three years, mostly in minority communities. But like other public programs and reinvestment agreements, it results from a concerted community effort to overcome past discrimination and does not serve as a measure of general fairness in the marketplace.

4. Finally, there are some technical issues that can actually screen out HMDA records of home improvements in white areas. For example, the HMDA computer tapes flag, and then screen out of reported totals, loans believed to be too large. In working on the studies in Atlanta with the Atlanta Journal and Constitution, I found that loans over $50,000 were often removed from the counts under the assumption that a loan that large could not be a home improvement loan. But loans this large are not uncommon for higher income homes - which are most often found in white areas. Thus, this process removes more white loans than minority loans.

These are some of the reasons why aggregate levels of home improvement loans may seem higher in many minority communities. Whether these levels in a given city are a result of biases in the data, or a greater need in the aging and often deteriorated housing stock made available to minorities, the data do not suggest equality in the market. They are simply another technique used by the financial regulatory agencies to avoid aggressive fair housing enforcement.

Attachment to the Statement of Calvin Bradford

NTIC National Training and Information Center
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FINANCIAL INSTITUTIONS FAIR PRACTICES ACCOUNTABILITY ACT
(Summary of National Peoples Action Proposal - August, 1989)

The provision of Federal deposit insurance for certain accounts in regulated financial institutions serves a dual purpose. First, it establishes an obligation on the part of the Federal Government to protect the deposits of the public, within legally defined limits. Second, it places on the institutions receiving the protection of deposit insurance an obligation to serve the convenience and needs of the community each lender serves. Deposit insurance is given to some institutions, and not others, precisely because these insured institutions are chartered to serve critical economic functions in our national economy.

In serving these needs, the Federal Government has placed a special emphasis on the need to avoid discrimination in the provision of these deposit and credit services; and it has placed upon these lenders an affirmative obligation to serve all the people within a lender's defined community, especially those people of moderate and low incomes. These obligations are defined in The Equal Credit Opportunity Act, the Fair Housing Act (as amended) and the Community Reinvestment Act. Compliance with these laws is equally as important as compliance with safety and soundness requirements.

No institution whose policies and practices are found to violate these laws shall be entitled to the continuation of insured deposits. Institutions may be found to have policies or practices violating one or more of the provisions of these laws either as the result of compliance examinations by the Federal agencies charged with enforcement of these laws or through successful litigation where the charges include violations of provisions of these laws.

In addition to any judgments and remedies specifically provided to the plaintiffs or plaintiff class, a legal judgement against a financial institution for the violation of any provision of these three laws shall also be deemed to be a finding of the violation of such provision for the purposes of regulation. As such, the Federal regulatory agency responsible for compliance examinations of the financial institution in regard to the provision that was violated shall take regulatory action.

The normal sanctions shall include the restructuring of the subject lending institution, holding company or service corporation, or the sale, merger, or liquidation of the subject institution resulting in the transfer of the insured deposits to another institution found to be in full compliance with these laws. Lesser sanctions can be imposed only in cases where the regulatory agency can demonstrate in a published review and analysis that the violations were so minor as to have had no significant effect on any of the protected populations defined by these acts and that the alternative remedies will insure future compliance.

Senator DIXON. Thank you, Mr. Bradford.

Well I want to go into the testing thing and a few other things with you folks, but let me first ask you. Mr. Fishbein, I'm embarrassed to say I don't remember which one of the regulators said they were talking to you about suggestions——

Mr. FISHBEIN. At various times, I guess, we've had conversations with all of them. I would not necessarily term them as, you know, high-level policy discussions; they've been at the midlevel, enforcement level, more than anything else.

Senator DIXON. Well if the regulators were going to ask Allen Fishbein, now look, what should we do, we've got these numbers here and Dixon's getting to be a pain in the posterior about this and we've got to find some way to do something about this, what would you tell them are the important things that they ought to do, simplisticly for the chairman here and others that will be reviewing shortly whether we ought to look at some legislation this year? What would you do?

RECOMMENDATIONS

Mr. FISHBEIN. Well specifically for the regulatory agencies, first and foremost we think each of the agencies needs to create a separate division which would have authority for examinations in the consumer compliance, fair lending, and CRA area.

Now I know there's been some discussion about a movement toward what they call fair lending or consumer specialists and the FDIC is moving in that direction, for example.

But I'm talking about separate divisions. And the key here organizationally is that the head of that division would report directly to the head of the agency.

And right now the way it works is that those examiners, the examiners that work on consumer and CRA and fair lending issues, are part of the broader safety and soundness and commercial exam. So their recommendations on policies, their recommendations on whether a bank's expansion application should be turned down because of their poor CRA record or fair lending record is not made directly to the chief regulator him- or herself.

And we think that the decision on these things ought to be made by the person who's appointed by the President and confirmed by the Senate and not by lower echelon bureaucrats who are responsible for the commercial examination process and often are quite hostile to consumer and fair lending compliance.

I think that would go a long way.

Senator DIXON. All right. That's No. 1. We talked about that last year.

I take it you're saying none are really doing that yet. They all kind of suggest they're doing something like that but you're saying no, no, not just some specialist in the organization, we want a separate——

Mr. FISHBEIN. Division.

Senator DIXON [continuing]. Distinct division.

Now would that be necessary in all the different regulatory agencies? Are you saying every one of them ought to have a separate distinct division on this?

Mr. Fishbein. Yes. We feel that that's absolutely necessary to create an equal status for this type of exam or the commercial exam.

Senator Dixon. And could that be done internally now with the number of people they have without putting on a whole lot of additional bodies?

I can just hear somebody saying, you know, this is going to cost a lot of money, we're going to have all these extra people, this is a time when we're trying to find ways to cut the budget——

Mr. Fishbein. Well what I'm proposing really shouldn't affect the number of examiners, it's where they're housed in the organizational structure and how high a priority they receive within each of these agencies. And we feel that in those areas it's just not sufficient.

The Federal Reserve Board perhaps goes the furthest because they have a Consumer Affairs Division. But even here the head of the division, as I understand it, cannot make a recommendation to the Board of Governors on whether an expansion application ought to be approved, denied or approved with conditions based on consumer issues. And that ought to change.

Senator Dixon. OK. What's the next thing after that—OK. That's No. 1.

Mr. Fishbein Point No. 2, the OTS is the only agency that never published nondiscrimination regulations under the Fair Housing Act. These are regulations that specifically prohibit savings institutions in this case from engaging in redlining practices and otherwise discriminating.

They also provide that each savings institution has to have on hand a copy of its underwriting criteria that it uses for qualifying people for loans and any individual could come into that institution and theoretically at least receive a copy of it, so you could measure how they were treating it against what they said was the institutionwide standard.

Now all these years later still OTS has been the only agency to adopt this nondiscrimination regulations. And we recommend that the banking agencies and the HUD be required to adopt similar types of regulations with respect to the institutions that they supervise.

Senator Dixon. OK. That's No. 2.

Mr. Fishbein. Well, third would be testing and having a testing program but, as I said, I don't think the regulators are likely to undertake that. We think that perhaps they should be required to provide financial support to an agency that did undertake this responsibility.

Senator Dixon. What kind of an agency?

Mr. Fishbein. Well I mentioned HUD and, you know, it's HUD's——

Senator Dixon. Mr. Bradford doesn't agree with you.

Mr. Fishbein. Well I think it's HUD by process of elimination more than anything else. All of us have been frustrated with enforcement by HUD as well over the years, but our feeling is that there have been signs at HUD that there is some seriousness about enforcement and they do have some experience in the testing area, mostly in rental and sales of housing, not so much in the lending discrimination area. But what we're recommending is that——

Senator DIXON. Do they have adequate funding now to do that?

Mr. FISHBEIN. Well I think——

Ms. SMITH. No, I don't think they do. Not to do the lending testing.

Senator DIXON. OK.

But we'll be talking about what kind of testing in a minute.

But No. 3, testing.

Mr. FISHBEIN. But I just really want to emphasize, and I think it's a point that all the witnesses share, is that what we really think is that HUD ought to be contracting with private fair housing agencies and public agencies that have the direct line experience with doing this kind of testing.

We're not suggesting necessarily that HUD as an agency undertake this testing itself——

Senator DIXON. Yeah.

Mr. FISHBEIN [continuing]. But that it be authorized to establish a program to contract with others.

Senator DIXON. Do we do that that way now, I can't remember, in connection with purchasing of real estate?

Ms. SMITH. Yes. HUD has under the FHIP program.

Senator DIXON. The FHIP and FHAP program. I heard about that.

Ms. SMITH. Yeah. It has another name in the movement, but I won't share it.

Senator DIXON. Don't tell me, no, we don't want to have the media have a problem with what we can print here.

Ms. SMITH. They are contracting directly with private fair housing centers and lawyers committees across the country to do rental and sales testing primarily and there are a few lending testing contracts.

Senator DIXON. OK. So there's precedent. All right. That's No. 3.

Mr. FISHBEIN. And a fourth item that I think is important, although it may not seem that way at first blush, is to have a much more systematic and detailed reporting to Congress on the activities that these agencies are engaged in and their efforts to spot discrimination in lending.

I think the information provided through these hearings has been tremendous, but there really needs to be direction that on an annual and an on-going basis the regulatory agencies have to submit specific detailed information about the number of instances of discrimination they find and how they've investigated that and ultimately how they have disposed of that.

And that kind of data out in the public domain and reminding Congress of its oversight responsibilities will serve as a reminder to the agencies that this is an issue Congress considers to be important and that they have to pay attention to.

Senator DIXON. OK.

Anyone want to add to that? Ms. White, you look like you do.

USE OF APPLICATION INFORMATION

Ms. **White**. They have a wealth of documentation there on applications withdrawn, processed, and they don't take advantage of it, they don't do anything with it. They will sit there and they'll massage it and it goes nowhere. At best, as examinations come up on a 2-year or a 3-year basis, they will use the application information to give direction to the examiner to go out and see whether there is a pattern or a practice of discrimination. Typically it is described away, explained away in some manner and nothing happens with regard to the variances that they might find in the pattern.

So that information, if an advocate were in the same position as the examiners, that information would either be filed on or it would be referred over to Justice but it would not be handled in the same way. So that information needs to be brought outside of the agency in such a way that there is a public review.

Senator **Dixon**. How can we ever get them to refer anything to Justice? There's been a suggestion we might finally do one after all these years.

Ms. **White**. I think referring to Justice or HUD is anathema within the bank regulatory agencies because they see themselves as protecting the institutions that they are providing services for. They see this as a management consultant process. And because they are charged with the responsibility of maintaining safety and soundness, they interpret that as protecting them from any kind of lawsuits because that, of course, would open the safety and soundness question up to examination and review and possible lawsuits might result in damages against the institution. So referring things over to Justice is just beginning that slippery slide which they do not wish to engage in.

The same thing when HUD comes in to investigate a bank, they just go crazy.

Senator **Dixon**. Ms. Smith, you were talking about what you've done in Toledo. I was kind of interested in the fact that it looks like—I don't mean this as a critique of others, but like you may be doing more there than most places. I even got the impression that you might even be receiving cooperation from many of the better institutions in your city.

And you say you are using testing there effectively, isn't that your testimony, and that you say you've had some lawsuits settled there—I made a note there were 15——

Ms. **Smith**. Yes.

Senator **Dixon**. Were the loan applicants actually paid some money where it was demonstrated that there was prejudice in the lending practices of certain institutions we'll permit to remain unnamed, is that right?

Ms. **Smith**. Yes. The lenders—We've been doing this for 10 years and the lenders have seen the wisdom of working with us instead of litigating against us.

And the testing that we've done has just been the prescreening, prequalifying kind of testing on a very limited basis, because our cases have been direct individual victims of discrimination and we didn't have to test to prove their case, we were able to prove their case once we got into the records of the lenders.

Or oftentimes after the first few lawsuits were filed, the attorneys would sit down and we would talk about the evidence on the appraisal report that was in front of us. And the bank presidents came in to sit down and said yes, that appears to be a discriminatory practice and some of them would eliminate those policies.

Some of them are repeat offenders, but it's not on the same practice. We kind of—they clear up this one practice and then we catch them doing something a little bit different or more sophisticated.

Senator DIXON. Do you think you've seen improvement in Toledo as a consequence of the things you do there?

Ms. SMITH. Yeah. But, you know, Toledo is still pretty segregated, but we're seeing more money coming in and the banks working with the neighborhood groups. Toledo is a lot smaller and we receive special funding from foundations to engage——

Senator DIXON. What—you mean some foundation, private foundation——

Ms. SMITH. Private—right to look into this issue.

Senator DIXON [continuing]. Funds that, do they.

Ms. SMITH. And the reason we started on this is because the real estate industry came to us and said, we're trying to show homes in all neighborhoods now, we're trying to market homes to whites in integrated and minority neighborhoods and vice versa, we can't get the loans.

So the real estate industry pointed out to us which lenders were participating in redlining practices or discriminatory appraisal practices. That cooperation made us successful in bringing lending litigation. In fact, real estate agents have been plaintiffs in the lawsuits that——

Senator DIXON. Yeah. Well, one of the things you're doing that sounds so successful to me, though I don't think we can legislate that kind of a result—you're getting some cooperation from institutions that in effect are giving you some files and things that help you. I don't know how we can do that.

What's the thing that's helped you the most from the standpoint of developing these cases independent of the cooperation of the institutions, is it testing or is it just the fact that you have lawyers that are cooperating?

ENFORCEMENT SUCCESSES

Ms. SMITH. It's probably mostly the previous enforcement successes, that the penalties, the severe monetary penalties; and the exposure, lenders really don't like public exposure on these practices because a lot of other victims will say that happened to me, too, and they'll come forward. But I think it's been the enforcement.

And when we're talking about testing, the Department of Justice—there's a bill that's pending about giving the Department of Justice money to do testing also. That may be useful because there are states in the south and the mountain states where there are no private fair housing centers to do testing in lending areas.

And, you know, I support the idea of HUD getting money to do the testing and we're thinking about whether or not we support the Department of Justice getting money to do testing and using qualified fair housing groups and public agencies who know how to do this.

Senator DIXON. Well that's OK. I sort of think, just observing this as one Senator, I don't know how others would feel about it, that if we could sort of pinpoint who has the responsibility for some of these things it might help. There's an awful lot of cover in all the regulators coming up here and everybody testifying about how much more they've done and I think we're doing more than they are and so forth. I think if in some of these cases we could just say yeah, but it's your job, it might help a lot.

I don't know whether it ought to be HUD or whether it ought to be Justice or what it ought to be, but if at least we could bring up here once a year somebody and say now this is your responsibility, how well are you doing, at least it might be a significant thing to have it resting in that house. Do you follow that?

Ms. SMITH. Yes.

Senator DIXON. Do you see the logic of it?

Ms. SMITH. Yes.

Senator DIXON. Maybe you all ought to give that some thought in view of the fact I see some division even among consumer groups, Mr. Bradford having said to Mr. Fishbein that he's all wet. [Laughter.]

Mr. BRADFORD. I think all of us commend this hearing process. Allen was right, that nothing does more to create compliance over the decade I've watched this than hearings like this, and I get feedback from a lot of agencies about that.

But I think the other side of it is it's so hard to wrestle any kind of compliance out of the agencies that it does seem valuable to give money—it just sounds like a strange thing for me to say—to HUD and to other agencies, maybe Justice, to encourage testing. In fact, HUD does support independent testing efforts because this will bring cases in to HUD and HUD now has the capacity to pursue them on its own and compel Justice to pursue them.

So the people who do care and who have shown the initiative in this process should get funding. Putting money in those programs by Congress is probably the most effective way, I think, of getting compliance.

Senator DIXON. OK. Thank you.

Incidentally, I mentioned just the fact of getting the appraisal; I presume you all agree with that. I'm told a lot of times they can't even get their appraisal and it's pretty hard to make a case when you can't even show what they appraised your house for, you know.

So I was pleased to see the regulators don't have any problem with that. Do you agree that that is an important thing, having the appraisal in hand? I would think as a lawyer that's important.

Mr. Fishbein gave four things; we have duly noted them. We will carefully review that.

Does anybody want to say No. 5, or anything like that or elaborate upon what Mr. Fishbein has said? I note that you all are nodding a little and apparently have some concurrence of opinion on this.

Ms. SMITH. I wanted to add that under the Housing and Community Development Act there are sanctions available for suspension and debarment of agencies working with HUD, FHA mortgage lenders and other people that if they are found in violation at the Fair Housing Act during an investigation they can be suspended. If a Federal court finds that they have violated the—the Fair Housing Acts, they can be disbarred from doing business with the Government. I think that that kind of sanction ought to be part of any legislation or recommendation or however you all do it here, I think that would make the regulators and the lenders take this more seriously than they do currently.

And just on the testing I wanted to tell you that the prescreening would be a valid case to make in court. In rental testing, we have—the fair housing movement in the country has had settlements over $200,000 where simply white and black testers went in to inquire if apartments were available and they were given differing information on availability or the black was told absolutely nothing was available and the white was shown units. Here in Washington, DC, they have secured settlements of over $200,000. That's a real deterrent to someone continuing to engage in that practice.

And last I think part of the success in Toledo was after those initial lawsuits that the local lenders—now we don't have any institution that's locally owned any more. But when they were, they came to us and we had a very good working relationship and did one-on-one training with their CRA and mortgage loan officers.

Our training is very different from what they get other places. It's very detailed. Oftentimes they're surprised that we're saying this particular policy, even though you apply it equally to everyone, is still discriminatory.

MINIMUM MORTGAGE LOAN AMOUNTS

And I heard the regulators saying well, you know, we're looking to see if the policies are applied equally. Well in fact they may be applied equally, but the policy itself may be discriminatory and I don't hear the regulators being able to identify that. A blatant example is the minimum mortgage loan amounts, that they apply that equally across the board, but it has a disparate impact on racial minorities. They don't see that as discrimination.

And that policy——

Senator **Dixon**. Can you suggest though that there shouldn't be some kind of minimum? Are you saying there shouldn't be?

Ms. **Smith**. Well because——

Senator **Dixon**. I'm just asking.

Ms. **Smith**. No, I think there should not be because there are cities all across this country—in my city—where you might have a house that's valued at $12,000 and it's a nice house. I know it's hard to believe around here but——

Senator **Dixon**. No, no, let me tell you, where I come from, that's not hard to believe.

Ms. **Smith**. Yeah. And you know maybe——

Senator **Dixon**. I could show you some pretty nice houses for $12,000 in certain places, believe it or not.

Ms. **Smith**. And maybe they're only putting down $3,000. And their income can't handle a loan that's 5 years or——

Senator **Dixon**. Well maybe that's fine. Maybe we'll think about that minimal question. I don't know. I'd want to tear around on that a little bit like a dog on a bone——

Ms. **Smith**. Well our lenders in Toledo have eliminated it.

Senator **Dixon** [continuing]. But you make a point there.

I can think of communities in my area where $12,000 is a pretty expensive home, believe it or not.

Ms. **Smith**. Right. Right.

Senator **Dixon**. I know that may sound shocking to people from big cities around America, but it's true.

Ms. **Smith**. But our lenders in Toledo have agreed not to have any minimum mortgage loan amounts at all in effect.

Senator **Dixon**. They do what now, Ms. Smith?

Ms. **Smith**. There are no minimum loan amounts.

Senator **Dixon**. In Toledo, there are no minimum loan amounts.

Ms. **Smith**. Right.

And we have negotiated ten year mortgage loans for a $10,000 loan if that's what the family needs to be able to be creditworthy or, you know, to meet the income-to-debt ratios, that they can adjust that in order to make home ownership available.

But we're also finding and I think the regulators—I don't know why they don't see this minimum loan amount as discriminatory. We have a savings and loan that has already been conditioned and they just issued a policy that they will not make any multifamily mortgage loans in the area and the regulators are saying that that may not be discriminatory. Well that is disinvestment and we're notifying the OTS in Cincinnati about that to see what they will do about it.

But those are policies. And examiners will come in and say, "Well that policy was applied equally across the board" and they fail to see that it has a disparate impact on minority families.

Senator **Dixon**. Yeah.

Anything else that you could add? Be reminded, we review this later and the ideas you suggest are things—I don't say we take every one of them but they're things we carefully evaluate. So I think I've noted five things that are worthy of very careful evaluation by us——

Mr. **Fishbein**. Mr. Chairman——

Senator **Dixon**. Mr. Fishbein.

Mr. **Fishbein** [continuing]. I mentioned it in my written testimony and it doesn't pertain directly to the regulators, but I think if there is an effort to do testing beyond the preapplication stage, there will need to be some changes in Federal law to permit that to happen.

Senator **Dixon**. Yes, I think Ms. Smith pointed that out and we're aware of that. I think you noted in my questioning of regulators I touched upon that, that obviously presents a little different problem than just going and trying to buy a place. Yeah. We note that.

I don't know quite how to handle it yet but I note it.

OK. Has everybody—have you vented your spleen on Mr. Fishbein sufficiently, Mr. Bradford? Are we all at rest now?

Senator DIXON. Thank you. We appreciate your coming. Adjourned.

[Whereupon, at 12:04 p.m., the meeting of the subcommittee was adjourned.]

[Response to written questions to the witnesses follow:]

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM

JOHN P. LAWARE

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

JOHN P. LAWARE
MEMBER OF THE BOARD

August 13, 1990

The Honorable Alan J. Dixon
Chairman
Subcommittee on Consumer and
Regulatory Affairs
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for your letter of June 12 containing follow-up questions to my testimony at the Subcommittee's **May 16 hearing** on mortgage discrimination. My answers to the questions you posed are enclosed.

Please let me know if we can be of further assistance.

Sincerely,

John P. LaWare

John P. LaWare

Enclosure

Governor LaWare subsequently submitted the following in response to written questions from Chairman Alan J. Dixon, in connection with the hearing held on May 16, 1990.

Q.1. In how many instances over the past three years has your agency found substantive violations involving mortgage race discrimination of the Fair Housing Act (FHA) or Equal Credit Opportunity Act (ECOA) while conducting examinations? Explain how each of these substantive violations was resolved.

A.1. Over the last three years 163 state member banks have been required to take corrective action for violations of the ECOA or FHA in accordance with the interagency supervisory enforcement policy. Less than 7 percent of the banks were cited for violations involving mortgage lending; each of these cases involve marital status discrimination, rather than racial discrimination. However, even though examiners have had difficulty establishing clear cut violations involving racial discrimination, it is not uncommon for them to raise questions with the bank about transactions to help assure that the bank is aware of its record and of its responsibility to treat customers in a non-discriminatory fashion.

When a substantive violation of the enforcement policy is found, the institution is required to correct the violation both retrospectively and prospectively. For example, if the violation involves an improperly required spousal signature on an obligation where the signature should not have been required, the bank must identify all the affected loan files and inform the individuals that the signator will be released unless that spouse wants to remain liable for the debt; and if the violation involves loan denial notices that are incorrect the bank must identify all affected individuals and send corrected notices to them. In either case, the bank is required to discontinue the illegal credit practice and train its employees regarding the provisions of the law.

Q.2. How many fair lending written complaints involving mortgage race discrimination did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation. Explain how each of these violations was resolved.

A.2. From January 1, 1987 through May 31, 1990 the System received a total of 275 complaints involving the Equal Credit Opportunity and the Fair Housing Acts against state member banks.

Of the 275 complaints only nineteen complainants alleged discrimination in mortgage lending. Of these complaints, two involved allegations of racial discrimination. Neither investigation conducted in these two cases found a substantive violation of law.

In one case, the seller of the property in question alleged that the potential buyer had been discriminated against by the bank on the basis of race. During an on-site investigation, we found that the bank had internally approved the potential borrower's application, subject to obtaining mortgage insurance as required by a bank policy applicable to all transactions involving a downpayment of less than 20 percent of the purchase price. Two mortgage insurance companies declined to provide the required insurance coverage. The bank responded by offering alternative approaches, including increasing the downpayment to 20 percent. Because the applicant did not respond to these offers, the bank did not approve the application. In responding to the complaint, we explained the situation and directed the complainant to the Federal Trade Commission, which supervises mortgage insurance companies, for any further investigation of the matter.

In the second instance, we found that the bank declined the application because it did not make the type of loan requested - a temporary construction loan - in the absence of a commitment by a lender to provide permanent financing. The applicant did not have such a commitment.

Q.3. The Toledo Fair Housing Center received 102 mortgage discrimination complaints over the past 3 years just from the Toledo area-- of which about 40 percent showed probable cause. How many mortgage discrimination complaints did you receive for the entire U. S.? Is the number roughly proportional to the Toledo experience? If it is significantly lower, what factors might account for the difference?

A.3. As indicated in our response to question 2 above, in the past three years, the System received 19 complaints about state-member banks which involved allegations of illegal discrimination in mortgage or home improvement lending, only 2 of which alleged racial discrimination.

There may be several reasons why the System receives few complaints about discrimination in mortgage lending. Many state member banks are located in small towns and do not offer mortgage loans on a wide scale. Our receipt of few complaints about mortgage discrimination may be due in part to this limited involvement of the banks we supervise in mortgage lending.

Proximity may also play a role in a potential complainant's decision about which agency to contact with a grievance. A consumer having a problem with a local bank may be more likely to contact a local consumer protection agency, or perhaps even a state banking or consumer protection authority, than a federal one.

Name recognition and association may be another factor. It would seem reasonable that persons believing they have been discriminated against may turn for recourse to those organizations readily identifiable as active in the civil rights area -- which would mean those with the words "fair housing", "human rights" or "equal opportunity" in their titles.

Q.4. How many hours out of an examination will an examiner spend on fair lending enforcement? How many hours on the Community Reinvestment Act (CRA)? How often are these exams done?

A.4. Attachment A presents a table showing the average number of hours spent on fair lending enforcement and CRA examinations over the last three years. We have provided a breakdown of time spent on these portions of the examination by bank asset size. It should be kept in mind that the majority of state member banks fall into the $25-100 million asset size category.

State member banks are examined, at a minimum, every 18 to 24 months under System examination frequency guidelines.

Q.5. In your exams, do you check whether certain minority neighborhoods have higher rejection rates than comparable white neighborhoods?

A.5. Our analysis primarily focuses on the treatment of individuals with different personal attributes -- such as sex, marital status, and race -- rather than on the "rejection rates" for the neighborhoods in which they live. To check for compliance with the ECOA, examiners gather from loan files and arrange on spreadsheets key "profile" information for both accepted and rejected loan applicants. They are then able to readily compare the characteristics (including income, credit history and level of debt) of those who received credit with those who were denied, looking for any differences in the way the bank's stated lending standards have been applied. Such an analysis can, and often does, reveal that certain classes of people have been rejected with greater frequency than others; for example, examiners may discover that female applicants are turned down more often than males. However, this does not end the inquiry. The examiner then attempts to determine whether the reason for the higher rejection rate was illegal discrimination. As such, the examiner's job is to determine whether credit decisions were consistently made in an even-handed manner, based on the credit-related qualifications of the applicants.

For those banks located in MSAs, examiners may also study the HMDA aggregation tables for a profile of housing-related lending according to income level and race, as well as other factors. The tables give a broad overview of lending patterns for individual lenders as well as the MSA as a whole, and can point to areas for further review with regard to extending credit in neighborhoods with specific race and income characteristics. HMDA data, prior to recent amendments contained in FIRREA, have not captured information regarding unsuccessful loan applicants, and therefore have not been suited to a comparison of rejection rates. In the future, however, it will be possible to perform such an analysis using the expanded HMDA data.

Q.6. What are your examiners trained to do when they find a lending institution with a policy of requiring a minimum loan size, lot size or income level? a maximum age of the house? that the neighborhood was stable or improving? How many institutions have been cited for this?

A.6. Virtually all financial institutions have standards and policies governing the types of property they are willing to finance, particularly in the real estate area. Those standards and policies are appropriate to the extent they are prompted by a legitimate business need, and reflect the credit risk the mortgage represents to the lender. To the extent they are derived from factors that do not predict risk, either reliably or at all, or are arbitrarily based on the location of the property, they may be inconsistent with the precepts of the fair lending laws if they have a disproportionate adverse impact on people with the characteristics protected by ECOA and FHA.

Examiners are trained to look for property underwriting criteria which are not demonstrably related to mortgage risk, and which limit the amount and type of credit available in less affluent or racially mixed neighborhoods. Clearly, underwriting criteria of the type you mention would flag the examiner's attention; of concern would be criteria such as minimum loan amounts which may be higher than the average cost of dwellings in a given neighborhood, arbitrary cutoff points in terms of age of property, and overly restrictive rules pertaining to the width or setback, for example, of the structure. In addition, examiners are trained to determine whether loan applications are evaluated on an individual basis or whether applications are rejected because the property is located (or the borrower lives) in an area containing other properties that the bank believes not to be suitable risks.

Examiners do often question whether certain underwriting policies and practices are justified by a business need, discuss with bank management their potential discriminatory impact on low- and moderate-income or minority persons, and strongly advise that the policies be reviewed and revised, when appropriate. These cases have generally not been considered violations as such in the examination report, because the facts and conclusions to be drawn from those facts are usually not clear cut. Factors relating to the market served and the banks' own internal cost and profitability structure often leave cases such as these in a posture of some doubt and debate.

Nevertheless, the existence and/or results of such policies have been drawn to banks' attention, generally in the form of an advisory comment, in the consumer compliance portion of the examination, and are likely to be strongly criticized from a CRA standpoint. Loan restrictions and minimum loan amounts were discussed in two of the redacted CRA examination reports provided to the Subcommittee last fall (Attachment B); both of these banks received low CRA ratings.

Q.7. If a loan were denied because of a low appraisal on the property -- as is often the case in minority neighborhoods -- will the examiner check this in its computerized sampling technique? Will the examiner be able to check whether the appraisal itself was based on illegal discrimination?

A.7. Examination procedures have been geared to alert examiners to any role excessively low appraisals may play in a bank's lending decisions. In examining for compliance with the Fair Housing Act, particular attention is given to such matters as whether the appraisal is done by bank personnel or by an independent appraiser; the qualifications of the appraiser; whether comparable properties or other justifications for establishing value are selected reasonably and used appropriately; the amount of appraisal fees; and whether there any circumstances in which an appraisal would not be ordered. In addition, appraisal forms are reviewed to determine whether such criteria as the age of the property and its style and size are utilized to accurately reflect market value. Further investigation would be triggered by any indication that the racial or ethnic composition of a neighborhood was taken into account in the appraisal process, as would the presence of any unexplained codes or ranking system, or references to such ambiguous qualities as "pride of ownership."

I believe these procedures are helpful, though not definitive, in checking for appraisals based on illegal discrimination. Our examiners are not trained as appraisers and, absent the type of more obvious matters indicated above, do not generally second-guess appraisals.

We are very concerned, nonetheless, about the possible role that appraisals may play in credit discrimination. As indicated in the appendix to my May 16 testimony, our examiners have occasionally noted appraisal practices which triggered an expanded review of bank practices.

In those instances banks were advised to change practices that may have had a discriminatory impact.

In June, the Board issued amended regulations pursuant to FIRREA which require that appraisals be performed in writing and in accordance with uniform standards. In particular, the new rules mandate that appraisals conform with the Uniform Standards of Professional Appraisal Practice, as adopted by the Appraisal Foundation. Those standards stipulate that "an appraiser must avoid stereotyped or biased assumptions relating to race, age, color, religion, gender or national origin or an assumption that racial, ethnic, or religious homogeneity is necessary to maximize value in a neighborhood. Further, an appraiser must avoid making an assumption or unsupported premise about neighborhood decline, effective age, and remaining life."

I would like to clarify the point that Federal Reserve examiners use statistical and judgmental sampling in various aspects of the compliance examination, rather than computerized sampling, to select and review loan files. Your question perhaps refers to the fact that some of our Reserve Banks use a software application developed for the personal computer to analyze the information about applicants gathered from the judgmental sample of loan files used in our credit discrimination analysis.

Q.8. Some regulatory agencies have testified that their examination techniques test for discriminatory practices by comparing rates of one financial institution with others in the same area. Do wide disparities exist between institutions? Give some examples (without revealing names). Various aggregate studies imply that lenders across the board may be discriminating. Would not this technique then suggest that no problem exists, when in fact there is a major problem?

A.8. Your questions seem to relate to the procedures we use to check for compliance with the CRA, particularly with regard to the geographic distribution of credit, rather than for detecting illegal credit discrimination. As I mentioned above in question 5, in investigating a bank's adherence to the fair lending laws, examiners use a case-by-case approach to compare an institution's treatment of various classes of applicants. This approach would not include comparing one institution's lending patterns or terms with those of another.

We may, however, make a comparison among institutions in assessing the geographic distribution of credit in connection with CRA performance. We have found it helpful to use HMDA data to compare the percent of mortgage and/or home improvement loans made by a given lender in low- and moderate-income (or predominately minority) neighborhoods, with the percent of loans made in those same neighborhoods by all reporting lenders. To a great extent this simply helps us to know whether the area involved is an active market, generally, for this type of lending, or is a relatively inactive one. We have also found it helpful, when comparing lending patterns in different census tracts, to calculate the number of loans made per owner-occupied unit. However, our inquiry does not end with the production of the relevant numbers and ratios, since we believe it is necessary to try to understand the reasons behind the numbers.

Redacted samples of such analyses were previously furnished to the Subcommittee. You will find in reading them that such comparisons yield very different results, depending on the institution and the environment in which it operates. In some cases, we did find that the record of a particular lender is significantly better, or worse, than that of other lenders in extending credit in less affluent or minority areas. The samples will also give you a sense of how important it is to factor into the analysis other information such as trends in the local economy affecting vacancy rates and residential sales, and the ratio of rental to owner-occupied housing.

You question the validity of this type of analysis, given that studies of aggregate lending patterns imply that all lenders may discriminate. As you know, we are not in agreement with the conclusion that the disparities shown to exist by the studies are necessarily the result of racial discrimination. The influence of other factors in the market surely play a role in shaping the lending patterns shown by the studies, including the frequency of housing turnover in the respective neighborhoods, the loan activity of mortgage bankers, the differences in loan products offered by commercial banks and other lenders, and factors other than income that affect individual creditworthiness.

It is also important to note that we use this type of analysis to assess one aspect of an institution's CRA performance -- the geographic distribution of credit. The results are weighed together with our review of an institution's efforts to ascertain community credit needs, to offer products which are responsive to some of those needs, to refrain from any illegal credit practices, and to participate in community development activities.

Q.9. No agency has referred cases of possible discrimination to the Department of Justice for prosecution. Have you referred any cases to the Department of Housing and Urban Development (HUD)?

A.9. No. As indicated in question 1, the cases of illegal credit discrimination which we have found in the area of mortgage lending have involved disparate treatment on the basis of marital status rather than race. Referral of such cases to HUD would not be appropriate, given that marital status is not one of the "protected classes" under the Fair Housing Act for which HUD has primary enforcement responsibility.

Q.10. HUD testified last October that the most effective way to detect discrimination is to gather the necessary data and to examine it for patterns of discrimination. What statistical information would prove or strongly suggest discrimination? Do you collect such information? If not, why not?

A.10. We do not believe that statistical information on aggregate lending patterns can prove or disprove that illegal discrimination has taken place, though it may provide a starting point for further inquiry. While such information can point to disparities which exist between the number of loans extended to whites versus minorities, analysis of the information sheds little light on why those disparities may exist. Because there are many reasons which may account for disparities other than illegal discrimination, it would not be appropriate to say that the information suggests discrimination, absent further study. A comparison of individual loan applications, as part of the examination process, is necessary to determine whether accepted and rejected loan applicants were, in fact, similarly qualified in terms of such factors as nature of credit history, length of employment and level of debt.

Under provisions of Regulation B which implements the Equal Credit Opportunity Act, banks are required to note the race or national origin, sex, marital status and age of persons applying for a loan which would be used primarily for buying or refinancing a home.[1] Compliance with this provision is checked during the course of examinations. The information obtained by banks, and retained in their loan files, is used by examiners in conducting the credit discrimination analysis portion of the examination to suggest areas for investigation. The information is not, however, collected centrally and aggregated because, for the reasons described above, we do not believe it would be particularly useful to do so. The Federal Reserve does, of course, collect the types of statistical information required by the Home Mortgage Disclosure Act. Since the enactment of HMDA, it has also acted as agent for the FFIEC in annually compiling the data submitted by all reporting lenders and in preparing aggregate tables which are made available to the public at central data depositories located in each metropolitan statistical area (MSA).

Q.11. Will the new statistical information to be gathered pursuant to the recently amended Home Mortgage Disclosure Act (HMDA) be sufficient to strongly suggest discrimination (assuming disparities are present in the data)? Will this data be more useful than existing HMDA data? Will you use it in any way different from existing HMDA data?

A.11. The expanded HMDA data will provide a better tool for focusing our efforts to detect illegal practices, given that the new reporting requirements enhance existing data in two important ways. First, the data will provide actual information as to the race, gender, and income of individual loan applicants. In the past, race and income information could be only roughly gauged by matching the loan transaction with the demographic characteristics of the census tract where the property involved was located. For example, existing data could indicate that a certain number of loans were made in low-income, predominately minority census tracts, but could not identify the race or income level of the person receiving the loan. A second benefit of the new data is that they are not limited to loans actually extended, but capture information about loan applications and their disposition - approval, denial, approved but not accepted, withdrawn by applicant, or closed by the institution for incompleteness.

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[1] For other types of loan transactions, capturing this information is not required and therefore would not be noted on the application.

The data will be used in much the same way they have in the past, but HMDA analysis will now present a much more detailed picture of individual and aggregate lending patterns. Our attention is likely to be focused on the revised aggregation tables, which present various cross-tabulations of loan applicant or census tract characteristics with information regarding the disposition of the application. Studying these tables will suggest where "gaps" may exist in an institution's lending, and enable us to identify where rejection rates for different classes of people may differ markedly and to target our loan applicant sample to those individuals that may be affected.

The expanded data will have some significant limitations which preclude it from being seen as more than a useful tool, however. Even with its important enhancements, the data will not enable us to detect possible illegal prescreening. Nor will it offer any insight on the possible explanations for the lending patterns exhibited, including some idea of the strength of consumer demand for housing-related credit, local economic and market factors, and the debt structure of a particular market segment -- all of which must be taken into account in determining whether aggregate patterns are the result of illegal discrimination or individual creditworthiness. Although one of the new HMDA tables will cross-tabulate characteristics of rejected applicants with the various reasons reported for credit denials, reporting this information is optional. Its completeness will vary from institution to institution, and its accuracy will likely be difficult, if not impossible, to verify.

Q.12. The Center for Community Change has recommended in its testimony that each regulatory agency should adopt regulations similar to the Office of Thrift Supervision's (OTS) non-discrimination regulation, which prohibits redlining and requires written loan policies to be made publicly available. The OTS believes that requiring all savings associations to make available to potential borrowers their clear, nondiscriminatory loan underwriting standards is an important safeguard to assure uniform application. What do you think of this idea?

A.12. We believe that having written policies in place is desirable to carry out management responsibilities effectively, and we strongly recommend that the banks we supervise develop written lending criteria. Nevertheless, we do not feel that it would be appropriate to impose such a requirement on all banks, nor do we see a significant benefit in requiring that underwriting criteria be made public.

Q.13. The National Fair Housing Alliance recommended in its testimony at both hearings that a brochure for mortgage loan applicants explaining how to recognize subtle acts of discrimination and how to file complaints be provided to every loan applicant who is rejected. Most of the regulatory agencies have indicated that new brochures for consumers would be useful. How much input will the agencies be getting from civil rights specialists in designing these brochures? How will they be different from past brochures? When will they be distributed and how? Will the brochures include phone numbers for the Justice Department's Civil Rights Division, HUD's Fair Housing and Equal Opportunity Division, and local public or private fair housing agencies?

A.13. In developing the text of the new brochure, Board staff solicited written input from the Community Affairs and Housing Subcommittee of the federal Consumer Advisory Council, whose membership includes individuals with expertise in the civil rights area as well as experience in working with lenders and the general public. A draft of the proposed text will be circulated to Council members for further comment as work on the brochure progresses.

This will be the first brochure published by the Board specifically addressing the issue of mortgage lending discrimination. It will seek to explain in clear terms what the potential borrower should expect in the application process, the types of qualifying information lenders typically request, and the types of questions the potential borrower should ask the lender. This information will be geared to alert consumers to subtle, potentially discriminatory lending practices, and will provide a list of enforcement agencies which can provide assistance if a potential borrower feels he or she has been discriminated against.

We anticipate that the brochure will be available in early fall 1990. To ensure distribution is as wide as possible, we will utilize our consumer mailing list and the consumer media as well as the Consumer Advisory Council, appropriate members of the Congress and the Federal Reserve Banks.

The brochure will provide the addresses and telephone numbers for Federal Reserve Banks, the other federal financial regulators and appropriate federal and state enforcement agencies. We plan to include a contact point at HUD in light of its responsibilities for handling complaints under the Fair Housing Act. The Justice Department's Civil Rights Division will not be listed, however, because we understand the Division does not respond to individual complainants. Finally, a listing of local public or private fair housing agencies would be far too lengthy to include in the brochure.

Q.14. Page 13 of your testimony states that you "have completed a detailed analysis of system enforcement activity involving serious violations of the Fair Housing and Equal Credit Opportunity Acts by reviewing our examination and consumer complaint data bases." What were some of the findings of this detailed analysis? What actions have been taken as a result?

A.14. The staff of the Division of Consumer and Community Affairs conducted a review of all instances where Reserve Banks required banks to take corrective action under the ECOA/FHA Enforcement Policy over the last 5 years. We were interested in knowing the number of cases where such action was required to correct the violations detected during the examination, and the number of cases where -- because such violations were part of a pattern or practice rather than an isolated occurrence -- banks were required to conduct a file seach to identify all affected applicants over the 24 months preceeding discovery of the violation (6 months in the case of inadequate credit denial notices), to take appropriate corrective action and also to ensure that the violations were not repeated in the future. Those results are given in Attachment C.

We also reviewed the means used by banks to complete the required corrective action, given that the Enforcement Policy does not prescribe a standard format for customer notification. Included in Attachment C are samples of letters sent by banks to affected customers. We have also had occasion to use other techniques to secure compliance with ECOA provisions. For example, in 1980 (prior to the adoption of the Enforcement Policy) the Board concluded in an Order that a bank was prescreening applicants and conditioned approval of the application upon the bank maintaining a register of all local applicants for at least one year. The Order is also included in Attachment C.

Our findings are further described under question 1 of this document, and in the appendix to the May 16 testimony.

Q.15. The Federal Financail Institutions Examination Council, the coordinating group of all the regulatory agencies, has been studying the idea of mortgage review boards, at least since its meeting last November 19. Your testimony describes with promise the Philadelphia Mortgage Plan. When will the Exam Council's study be completed? When will its findings be implemented?

A.15. The Exam Council has looked at those mortgage review boards which have been successful in providing an appeals process for rejected mortgage credit applicants. The Council has now turned its attention to those review boards which have not been very successful, in order to try to identify the pitfalls such arrangements have encountered and what combination of elements make their operations most effective. We anticipate our study will be completed in the next few months.

Q.16. In FIRREA Congress attempted to expand HMDA to all mortgage lenders (making more than five loans in a metropolitan statistical area). The Federal Reserve subsequently issued regulations saying that only mortgage bankers with more than $10 million in assets are required to keep HMDA data. Testimony from the Center for Community Change claims that these regulations exempt all but about three dozen mortgage companies from HMDA. Do you agree with the Center's figures? Is not the objective most consistent with Congressional intent to make HMDA broadly applicable to all lenders, including mortgage bankers?

The Board was aware, when it revised Regulation C in December 1989 to implement the amendments to HMDA in FIRREA, that most mortgage companies are excluded from coverage because of the $10 million asset test. The Board was constrained from establishing more complete coverage, however, by the language of the Home Mortgage Disclosure Act. Section 309 of HMDA exempts from coverage those depository institutions that have $10 million or less in assets -- even if they have a branch office in an MSA. The term "depository institution," in turn, is defined in section 303(2) of the act, as amended, to include "other lending institutions" such as mortgage companies.

The Board made a conscious effort to expand the coverage of mortgage bankers as much as legally possible by providing in Regulation C that the $10 million asset test applies to the combined assets of a mortgage company and any parent institution. We believe that this application of the test to combined assets brings within the disclosure requirements at least those companies most heavily engaged in mortgage lending. The Board does not have any data, however, that would enable us to establish the actual number of mortgage companies that are covered, but the effect of the statutory exemption is to exclude many such companies.

Q.17. You testified, "Non-affiliated mortgage lenders who are typically more active in minority neighborhoods...[are not] included in this data. That will be in the new HMDA data." Why do you believe that unaffiliated lenders would be more active in minority neighborhoods? The Boston Federal Reserve study released in September 1989 concluded: "...even including mortgage companies, overall mortgage lending in Boston is lower in black neighborhoods than in comparable white neighborhoods... the independent mortgage companies have fairly constant ratios across neighborhoods, which means that these institutions as well lend less in black neighborhoods than in comparable white neighborhoods."

A.17. Numerous studies have supported the finding that mortgage bankers extend a substantial proportion of the home purchase loans originated in predominately minority neighborhoods, but account for a smaller share of the market in white areas of similar socio-economic status. For example: Glenn B. Canner, "Redlining and Mortgage Lending Patterns," Research in Urban Economics, vol. 1, 1981, pp. 67-101; Robert B. Avery and Thomas M. Buynak, "Mortgage Redlining: Some New Evidence," Economic Review, Federal Reserve Bank of Cleveland (summer 1981), pp. 18-32; George J. Benston and Don Horsky, "Redlining and the Demand for Mortgage in the Central City and Suburbs," Journal of Bank Research (summer 1979), pp. 72-87; Peter M. Hutchinson, James R. Ostas, and J. David Reed, "A Survey and Comparison of Redlining Influences in Urban Mortgage Lending Markets," AREUEA Journal, vol. 5, 1977, pp. 463-72.

Further documentation comes from the 1988 newspaper series on mortgage lending in Altanta and Detroit. For example, the "Color of Money" series which appeared in the Atlanta Constitution indicated that 52 percent of home loans in the middle income black neighborhoods were FHA or VA-insured, while only 13 percent were of this type in the white areas of comparable income. According to the articles, few of these government-insured loans were made by banks or thrift institutions.

The reason for the greater level of activity by mortgage bankers in mostly minority neighborhoods is linked to the fact that, nationwide, mortgage bankers are involved in making government-backed home purchase loans to a much greater degree than commercial banks and thrifts. In 1986, for example, mortgage bankers originated over 85 percent of FHA-insured and VA-guaranteed loans made nationally that year. This is coupled with the finding that households purchasing homes in predominately minority neighborhoods are more likely to use a government-insured than a conventional mortgage instruments, apparently due to factors related to individual borrower characteristics, the lower downpayments required under these loan programs, and the fact that the purchase price of properties in those neighborhoods tend to fall within FHA ceilings.

We believe that the case of Boston is an aberration that may be explained by the fact that housing values in the Boston metropolitan area generally exceed FHA ceilings, and therefore preclude extensive government-backed mortgage lending activity. We would expect to see similar results in other high housing-cost areas.

Q.18. Years ago, the Federal Reserve Board had authorized the regional Reserve Banks to use testers, if they so desired. Have any Reserve Banks actually used testers? Would not testers be more efficient than examining reams of statistics?

A.18. In 1984, the Board decided against the routine use of testers in examining for illegal credit discrimination by state member banks. However, it did indicate that when there is a strong suspicion of possible discrimination, the Reserve Bank should report the facts and, in concert with Board staff, determine if using testers would be appropriate. I am not aware of any instances where testers have actually been used.

We believe that testing could be helpful in detecting illegal credit discrimination, but its usefulness is limited by two key constraints. First, the use of testers would simply not be feasible in the small rural towns where most of our state member banks are located, given that the bankers are very often personally acquainted with their customers, if not everyone in town, making it difficult to use testers who are nonresidents of the community. Second, when it comes to home purchase credit, as a practical matter the use of testing would have to be confined to assessing the treatment of prospective mortgage applicants at the pre-application stage of the lending process. To go beyond the pre-application stage would present significant costs and other obstacles connected with arranging for testers to go through the mortgage decision process -- for example, the need for a verifiable credit history maintained by a third party credit bureau, an appraisal with all the costs it would entail, a contract of sale on the home being "purchased" which in all respects would appear legally binding, and underlying documents to nullify the "sale" which was purportedly being financed.

Q.19. Attached to Calvin Bradford's testimony is an addendum arguing that a higher level of home improvement loans in minority communities is not evidence of a lack of discrimination. If you disagree with any of his contentions, please comment.

A.19. Point 1A of the addendum states that FHA Title I home improvement loans reported under HMDA are actually used for a variety of purposes. Mr. Bradford believes that a home improvement loan is one of the few sources of credit available to minorities, and so it is used for many other of their credit needs.

We are well aware that home improvement loans are widely used by both whites and minorities for purposes other than home improvement. As stated in an article which appeared in the Federal Reserve Bulletin last May (Attachment D) on page 337, surveys have found that traditional home improvement loans have historically been used by consumers to repay other debts as well as to finance home improvements. The regulation implementing HMDA stipulates that lenders report any loan, including a refinancing, whose proceeds as stated by the borrower at the time of the loan application are to be used for home improvement purposes, and that are recorded on the bank's books as a home improvement loan. Regardless of the ultimate use to which the credit is put, the fact remains that more home improvement loans are made per housing unit in predominately minority areas than in predominately white areas with similar incomes. For example, I would refer you to the Federal Reserve's analysis of the "Color of Money" series (Attachment E).

Point 1B states that there has been a shift toward the use of home equity lines of credit, the marketing of which has been generally targeted to affluent, largely white communities. Because these home equity lines are frequently used by white, middle class borrowers for purposes other than home improvement, the result is that borrowing against equity in mostly white neighborhoods tends to go unreported under HMDA, while the more traditional form of home equity borrowing almost always gets reported as home improvement lending in minority areas. We believe Mr. Bradford may be right to some extent, although we would note that most creditors advertise lines of credit in general circulation newspapers that reach all consumer groups. Moreover, the Board's recent consumer surveys indicate that both traditional home equity loans and the newer lines of credit are used by roughly similar proportions of minority homeowners (see Attachment D, page 336). The difference made by the increased popularity of home equity lines of credit beginning in 1986 is clearly not as great as Mr. Bradford would suggest. In studying home improvement lending data as far back as 1981 and up through 1986, we can see roughly the same magnitude of disparities in favor of minorities. That is, even before home equity lines of credit started attracting keen consumer interest in the mid-1980s, traditional forms of home improvement loans were extended with greater frequency in minority than in white neighorhoods. Once again, see the Federal Reserve Board's analysis of the "Color of Money" series for evidence of this point (Attachment E).

Mr. Bradford's assertion under point 4 is not correct. He indicates that loans over $50,000 are removed from the counts of home improvement loans under HMDA under the assumption that a loan that large could not be a home improvement loan. The procedure followed by Board data processing staff is to flag those home improvement loans reported as over $300,000. The Reserve Banks are then asked to verify the accuracy of any such reported loans; they are assumed to be correct if we are unable to receive confirmation in a specified time period. Therefore, the technical aspects of the data collection process do not discount the effect of the larger home improvement loans made most often in nonminority areas.

Q.20. Calvin Bradford testified, "It seems to me that the lowest mark of the lack of applying the effects test comes from the application that actually started the Atlanta Constitution studies: an application by SunTrust. It was challenged on the grounds that they had developed only one mortgage product that was clearly not attractive to minorities and that they had closed a branch in minority neighborhoods. The bank responded to the Federal Reserve that the effects test should not be applied to their chosen policies and practices, and the Federal Reserve responded by granting their application with no conditions." Please confirm these facts outlined by Mr. Bradford and explain the rationale for the Federal Reserve's actions.

A.20. The Federal Reserve System handled three bank holding company applications involving SunTrust Banks, Inc. (Atlanta, GA), between 1986 and the time the Atlanta Constitution articles were published. In none of these cases does the record indicate a fact situation such as the one Mr. Bradford described.

Attachment F is a Board Order dated November 26, 1986, approving an application by SunTrust Banks, Inc. ("SunTrust"), to acquire Third National Corporation (Nashville, TN). The application was protested on CRA grounds by Miami Legal Services, which had raised concerns about SunTrust's record in meeting the credit needs of low- and moderate-income and minority persons in its Florida services areas. In reviewing the record, the Board took into account SunTrust's record of serving its local communities in the state of Georgia, its private meetings with the protestant and agreement to work with it in developing a corporate CRA policy, as well as a number of commitments to enhance its CRA performance in Florida. As outlined in the Order, SunTrust committed to provide its Florida personnel more extensive training in consumer compliance, develop a policy on basic banking services for the organization, and improve its marketing of services in low- and moderate-income and minority areas. Moreover, it pledged to replicate in Florida some of the CRA-related services which have proven successful in Georgia (e.g., assistance to minority businesses and conservation of low-income housing). The Order contained provision for monitoring of progress in fulfilling these commitments through reporting to the Federal Reserve Bank of Atlanta.

In late 1987, SunTrust's application to acquire a denovo bank to process credit cards was protested by the Altanta Community Reinvestment Alliance, criticizing the CRA record of SunTrust's lead bank in Georgia, Trust

Company Bank ("Bank"). The Alliance alleged that Bank redlined low- and moderate-income and minority neighborhoods, did not participate in government-assisted loan programs, failed to offer basic banking services to non-elderly customers, did not adequately market its services in less affluent areas and failed to fund a community development corporation. In a meeting arranged by the Reserve Bank, Bank and the Alliance endeavored to work out their differences; some progress was made but the protest was not withdrawn. The Board found that CRA considerations presented by the case were consistent with approval, based on its review of the applicant's CRA record in Georgia and its compliance with the CRA commitments it had made to the Board the previous year. Accordingly, the application was approved by the Secretary of the Board on delegated authority in December of 1987.

SunTrust's January 1988 application to acquire Commercial Bank (Panama City, FL) was also the subject of a CRA protest. Comments were received from Direct Involvement Savannahians Together Urging Responsive Banking Services (DISTURBS), alleging that Trust Company Bank of Savannah ("Savannah Bank") failed to ascertain and meet the credit needs of low- and moderate-income neighborhoods of Savannah, failed to adequately market its services to those areas, made minimal efforts to support small businesses, discriminated against women and minorities, and had inconvenient branch locations and hours of operation in low- and moderate-income neighborhoods. As explained in the Order dated April 12, 1988 (Attachment G), the Board considered these charges in light of the Savannah Bank's most recent report of CRA examination conducted by the Comptroller of the Currency, SunTrust's response and several commitments offered by SunTrust to strengthen its service in Savannah. These included increased marketing and outreach efforts in low- and moderate-income and minority communities, the pursuit of community development opportunities with the city government, and stronger compliance with the consumer laws by all its bank subsidiaries. These commitments were also made subject to monitoring, through quarterly progress reports, to the Federal Reserve Bank of Atlanta.

ATTACHMENT A

FEDERAL RESERVE SYSTEM
Average Number of Hours Spent on Fair Lending
Portion of Examination (Fair Housing Act and Equal Credit Opportunity Act)

Bank Asset Size (in Millions)	1987	1988	1989
< 25	10	12	17
25-100	12	14	14
100-500	24	24	29
> 500	123	78	94

Average Number of Hours Spent on CRA Examinations

Bank Asset Size (in Millions)	1987	1988	1989
< 25	5	7	11
25-100	7	9	11
100-500	15	13	25
> 500	72	55	99

ATTACHMENT C

Final Report as of 4/18/90

Corrective Action Taken By State Member Banks In Accordance With ECOA/FHA Enforcement Policy

	Federal Reserve System	1989	1988	1987	1986	1985	1984
1.	Total Consumer Affairs Examinations Conducted	616	639	614	653	785	731
2.	Number of State Member Banks Taking Corrective Action*	48	65	49	66	57	55
3.	Number of State Member Banks Completing a File Search	32	43	29	34	46	47

* Item 2 exceeds Item 3 because banks are asked to correct all violations discovered during examinations, but only asked to complete a file search if it is determined that the violation actually detected is likely to be the result of bank practice.

Bank
Michigan

December 01, 1989

Dear :

Upon review of our Commercial Loan Portfolio, it was brought to our attention that need not be required to be contractually liable for the contract number between & and The Bank.

Should we not recieve instructions that should in fact remain on said contract within 30 days from the date of this letter shall be released from any and all contractual liability of this debt.

Sincerely,

Vice President
Compliance Officer

— MAIN OFFICE OFFICE :

(Date)

TO: CARDHOLDERS

According to our records, you have been issued more than one credit card on your account. We are currently revising our method of credit reporting in order to furnish information concerning the credit history of a spouse who is an authorized user of the account.

Separate information concerning your spouse's participation in your account has not been furnished to credit bureaus. In some instances this absence of information may have been a cause of your spouse's inability to obtain credit. If a user spouse has had a credit application declined, she or he may want to reapply.

IF YOUR SPOUSE HAS BEEN PERMITTED TO USE YOUR MASTERCARD OR VISA ACCOUNT, PLEASE COMPLETE THE BOTTOM OF THIS FORM AND RETURN IT TO US IN THE ENCLOSED PREPAID, PREADDRESSED ENVELOPE. THIS WILL ALLOW US TO CORRECTLY REPORT THE CREDIT HISTORY OF THE USER SPOUSE.

Account Number____

Your Name____
Please Print

Your Address____
Please Print

Your Social Security Number__________________________

Your Spouse's Full Name______________________________
Please Print

Your Spouse's Social Security Number__________________

CONFIRMATION LETTER

August 30, 1989

Loan #__________________
Date of Obligation 11-21-88
Amount __________________

Dear Ms. :

In reviewing your loan file and related documents, we found that your signature is not on the application (or financial statement) even though it appears on the debt instrument (note or guaranty). We wish to confirm your intent with regard to jointly applying, or being a guarantor, for this credit. Therefore, please sign in the appropriate space below and return this letter to me within 30 days, or by no later than September 30, 1989.

1. ________________________ I intended to apply as joint applicant (or a guarantor) and to be obligated on this loan.

2. ________________________ Although I signed the note (or a a guaranty), I did not intend to be an applicant, or to be obligated on this loan.

For your information, if you signed in space #2, you will be released from the note (or guarantor) although _______________ will remain obligated. Also, if we do not hear from you within 30 days, or by no later than September, 30, 1989, we must assume that you did not intend to be obligated on the above loan, and you will, therefore, be released from the note (or guaranty) in that event as well.

I appreciate your assistance in correcting our loan records. If you have any questions, please do not hesitate to contact me.

Sincerely,

Vice President

cc:

10/31/85

[Reg B Compliance Letter]

Dear Mr. _____________:

An examination of your credit file has revealed an inconsistency between your loan application and your loan documentation with respect to whether your spouse was intended to be [a guarantor] [a joint obligor] of the loan referenced on the attached Information Statement.

Please complete the enclosed Information Statement and return it to us within 30 days. Should we not receive a completed Information Statement from you prior to the expiration of such time period, we shall release your spouse from her [debt obligation] [guaranty], but only upon your substitution and our acceptance of a suitable alternate creditworthy party to provide the necessary credit to maintain the loan. Your spouse will be informed of the effective date of such release, provided a suitable substitute is accepted by us. If you have not provided a suitable substitute for your spouse within 60 days of the date hereof, your spouse shall not be released from her [debt obligation] [guaranty of the loan].

Very truly yours,

INFORMATION STATEMENT

Name and Address of Borrower(s):

Name and Address of Guarantor(s):

Date of Loan

Original Amount of Loan

Current outstanding balance of Loan

We hereby certify to [redacted] & Trust Company as follows:

☐ Each of the individuals listed above as a borrower and/or guarantor of the debt obligation referred to above intends to be bound as an obligor or guarantor, as the case may be be, of such debt obligation.

☐ The following individual listed above as a borrower or guarantor of the debt obligation referred to above did not intend to be bound as an obligor or guarantor, as the case may be, of such debt obligation:

Enclosed is a personal financial statement of ________________________________, for your consideration as a suitable alternate creditworthy party to provide the necessary credit to maintain the loan in substitution of the individual listed above.

Note: All borrowers and guarantors of the above-referenced credit facility must sign this information statement.

____
(Borrower)

____
(Borrower)

____
(Guarantor)

____
(Guarantor)

October 4, 1985

Re: Home Improvement Loan Account No.

Dear Customer:

As required by Regulation B implementing the Equal Credit Opportunity Act, we hereby terminate, this date, the Guarantee of all Liability signed by the below named non-applicant spouse of the obligations to [redacted] of the above-described borrower.

Name of Guarantor	Date of Guarantee of All Liability

If you have any questions regarding this notice, please contact the undersigned. Thank you for your attention in this matter.

Very truly yours,

[redacted]

approval of this proposal would result in undue concentration of resources, decreased or unfair competition, conflicts of interest, unsound banking practices, or other adverse effects on the public interest. Accordingly, the Board has determined that the balance of the public interest factors it must consider under section 4(c)(8) of the BHC Act is consistent with approval of these applications.

On the basis of the record and commitments made by Applicants and their principals, and for the reasons summarized above, the Board has determined that the applications under sections 3 and 4 of the BHC Act should be and hereby are approved. The banking acquisition shall not be consummated before the thirtieth calendar day following the effective date of this Order, and neither the banking acquisition nor the nonbanking acquisition shall occur later than three months after the effective date of this Order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of San Francisco, acting pursuant to delegated authority. The determination with respect to Applicants' nonbanking activities is subject to all of the conditions set forth in Regulation Y, including sections 225.4(d) and 225.23(b) (12 C.F.R. §§ 225.4(d) and 225.23(b)), and to the Board's authority to require such modifications or termination of activities of a holding company or any of its subsidiaries as the Board finds necessary to assure compliance with, or to prevent evasion of, the provisions and purposes of the BHC Act and the Board's regulations and orders issued thereunder.

By order of the Board of Governors, effective November 3, 1986.

Voting for this action: Chairman Volcker and Governors Johnson, Angell, and Heller. Absent and not voting: Governors Wallich, Rice, and Seger.

JAMES MCAFEE
Associate Secretary of the Board

[SEAL]

SunTrust Banks, Inc.
Atlanta, Georgia

Order Approving Acquisition of a Bank Holding Company

SunTrust Banks, Inc., Atlanta, Georgia, a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (12 U.S.C. § 1841 *et seq.*) ("Act"), has applied for the Board's approval under section 3(a)(3) of the Act (12 U.S.C. § 1842(a)(3)), to acquire Third National Corporation, Nashville, Tennessee ("Company"), and thereby indirectly acquire its twelve subsidiary banks.[1] Applicant has also applied under section 4(c)(8) of the Act (12 U.S.C. § 1843(c)(8) and section 225.23(a)) of the Board's Regulation Y (12 C.F.R. § 225.23(a)(2)) to acquire the following nonbank subsidiaries of Company: Third National Financial Services, Nashville, Tennessee, and thereby engage in mortgage banking including making, acquiring or servicing loans; Third National Insurance Company, Chattanooga and Nashville, Tennessee, and thereby underwrite credit life, accident and health insurance for Company and its subsidiaries; ThirdData, Nashville, Tennessee, and thereby provide data processing, data transmission services and data bases primarily to financial institutions; Third National Brokerage Services, Chattanooga, Nashville, Knoxville and Johnson City, Tennessee, and thereby provide securities brokerage services, related securities credit activities and incidental activities such as custodial services, individual retirement accounts and cash management services; and Third National Trust Company, Chattanooga, Tennessee, to engage in activities of a fiduciary, agency or custodial nature. These activities have been determined by the Board to be closely related to banking and permissible for bank holding companies under section 225.25(b)(1), (3), (7), (8) and (15).

Notice of the applications, affording an opportunity for interested persons to submit comments, has been given in accordance with sections 3 and 4 of the Act. (51 *Federal Register* 26,191 and 26,468 (1986)). The time for filing comments has expired, and the Board has considered the applications and all comments received, including comments in opposition to the applications from Legal Services of Greater Miami ("Legal Services"), in light of the factors set forth in section 3(c) of the Act (12 U.S.C. § 1842(c)), and the considerations specified in section 4(c)(8) of the Act.

Applicant is the second largest banking organization in Georgia, with total Georgia deposits of $5.2 billion,[2] representing 15.3 percent of the total deposits in commercial banks in the state. Applicant is also the second largest banking organization in Florida, controlling deposits in that state of $2.2 billion, representing 6.3 percent of the total deposits in commercial banks in Florida. Company is the largest banking organization in Tennessee with total deposits of $4.2 billion, representing 14.4 percent of state deposits.

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[1] Applicant also has applied to exercise a Warrant purchased from Company to acquire up to 24.9 percent of Company's shares. By its terms, the Warrant is exercisable only on the occurrence of certain events which include a material breach by Company of the merger agreement entered into with Applicant, or a tender offer, purchase, merger or filing by any person or group that would result in that person or group controlling at least 24.9 percent of Company's shares.

[2] All banking data are as of June 30, 1986.

conservation of low-income housing. In this regard, the Board notes that Applicant has a strong record of meeting the needs of the communities it serves in Georgia. Finally, Applicant will file detailed reports of its programs in order that the Federal Reserve System may evaluate Applicant's progress in meeting its CRA objectives.

The Board has carefully reviewed the records of Applicant, and Company as well, in meeting the convenience and needs of all segments of their communities. Based on this review and after taking into account Applicant's commitments to enhance its service to meet the convenience and needs of its community, including low- and moderate-income segments, the Board concludes that convenience and needs considerations are consistent with approval of this application.[7]

Applicant has also applied, pursuant to section 4(c)(8), to acquire the following nonbank subsidiaries of Company, all located in Tennessee: Third National Financial Services, Nashville, and thereby engage in mortgage banking including making, acquiring or servicing loans; Third National Insurance Company, Chattanooga and Nashville, and thereby underwrite credit life, accident and health insurance within the Third National system; ThirdData, Nashville, and thereby provide data processing, data transmission services and data bases primarily to financial institutions; Third National Brokerage Services, Chattanooga, Nashville, Knoxville and Johnson City, and thereby provide securities brokerage services, related securities credit activities and incidental activities such as custodial services, individual retirement accounts and cash management services; and Third National Trust Company, Chattanooga, to engage in activities of a fiduciary, agency or custodial nature. Because Applicant and Company do not compete in any of the same markets, approval of these applications will have no significant effect on competition in any relevant market. Furthermore, there is no evidence in the record to indicate that approval of this proposal would result in undue concentration of resources, decreased or unfair competition, conflicts of interests, unsound banking practices or other adverse effects on the public interest. Accordingly, the Board has determined that the balance of the public interest factors it must consider under section 4(c)(8) of the Act is favorable and consistent with approval of the application to acquire Company's nonbanking subsidiaries.

Based on the foregoing and other facts of record, the Board has determined that the applications under sections 3 and 4 of the Act should be and hereby are approved. The acquisition of Company shall not be consummated before the thirtieth calendar day following the effective date of this Order or later than three months after the effective date of this Order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of Atlanta, pursuant to delegated authority. The determinations as to Applicant's nonbanking activities are subject to all of the conditions contained in Regulation Y, including those in sections 225.4(d) and 225.23(b)(3) (12 C.F.R. §§ 225.4(d) and 225.23(b)(3)), and to the Board's authority to require such modification or termination of the activities of a holding company or any of its subsidiaries as the Board finds necessary to assure compliance with the provisions and purposes of the Act and the Board's regulations and orders issued thereunder, or to prevent evasions thereof.

By order of the Board of Governors, effective November 26, 1986.

Voting for this action: Vice Chairman Johnson and Governors Rice, Seger, and Heller. Absent and not voting: Chairman Volcker and Governors Wallich and Angell.

BARBARA R. LOWREY
[SEAL] *Associate Secretary of the Board*

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[7] Legal Services has also requested that the Board order a public meeting to receive public testimony on the issues presented by these applications. Although section 3(b) of the Act does not require a formal hearing in this instance, the Board may, in any case, order a formal or informal hearing. In the Board's view, the parties have had ample opportunity to present their arguments in writing and to respond to one another's submissions. In light of these facts, the proposals by Applicant to expand its services, and other facts of record, the Board has determined that a hearing would serve no useful purpose. Accordingly, Legal Services' request for a public hearing is hereby denied.

ATTACHMENT G

FEDERAL RESERVE press release

For immediate release

April 12, 1988

The Federal Reserve Board today announced its approval of the application of SunTrust Banks, Inc., Atlanta, Georgia, and Sun Banks, Inc., Orlando, Florida, to acquire Commercial Bank In Panama City, Panama City, Florida.

Attached is the Board's Order relating to this action.

Attachment

FEDERAL RESERVE SYSTEM

SunTrust Banks, Inc.
Atlanta, Georgia

Sun Banks, Inc.
Orlando, Florida

Order Approving Acquisition of a Bank

SunTrust Banks, Inc., Atlanta, Georgia, and Sun Banks, Inc., Orlando, Florida (together, "SunTrust"), bank holding companies within the meaning of the Bank Holding Company Act of 1956, as amended (12 U.S.C. § 1841 et seq.) ("Act"), have applied jointly for the Board's approval under section 3(a)(3) of the Act (12 U.S.C. § 1842(a)(3)), to acquire all of the voting shares of Commercial Bank In Panama City, Panama City, Florida ("Commercial Bank").

Notice of the application, affording an opportunity for interested persons to submit comments, has been given in accordance with section 3 of the Act. (53 Federal Register 179 (1988)). The time for filing comments has expired, and the Board has considered the application and all comments received, including comments in opposition to the application from Direct Involvement Savannahians Together Urging Responsive Banking Services ("DISTURBS"), in light of the factors set forth in section 3(c) of the Act (12 U.S.C § 1842(c)).

SunTrust controls fifty-two bank subsidiaries in Florida, Georgia and Tennessee. SunTrust is the second largest banking organization in Florida, controlling deposits in that state of $11.5 billion, representing 13.3 percent of the total deposits in commercial banks ("total deposits") in Florida.[1] Commercial Bank controls $166.9 million in total deposits in the state of Florida, representing 0.2 percent of total deposits in the state. As part of this proposal, SunTrust intends to acquire Lynn Haven Commercial Bank, Lynn Haven, Florida ("Lynn Haven Bank"), and Springfield Commercial Bank, Springfield, Florida ("Springfield Bank"), through bank-to-bank mergers with Commercial Bank. The Lynn Haven Bank, Springfield Bank and Commercial Bank (together "Banks") are under common management and ownership. After the merger of Lynn Haven Bank and Springfield Bank into Commercial Bank, SunTrust will control deposits equalling $11.7 billion, representing 13.5 percent of commercial deposits in Florida. Consummation of this proposal will have no significant effect upon the concentration of commercial banking resources in Florida.

The Banks to be acquired operate in the Bay County banking market.[2] SunTrust does not operate in this market, and thus, consummation of the proposal would not eliminate any substantial existing competition between SunTrust and Banks in

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1/ Deposit data are as of September 30, 1987.

2/ The Bay County banking market is approximated by Bay County, Florida.

the Bay County market. In addition, consummation of the proposal would not substantially lessen probable future competition in any market.

The Board considers the financial and managerial resources of SunTrust, its subsidiary banks and Commercial Bank to be consistent with approval of the application.

In considering the convenience and needs of the communities to be served, the Board has also taken into account SunTrust's record under the Community Reinvestment Act (12 U.S.C. § 2901 _et_ _seq_.) ("CRA"). The CRA requires the Board, in its evaluation of a bank holding company application, to assess the record of an applicant in meeting the credit needs of the entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation. The Board has received comments from DISTURBS, which represents low-income groups and individuals in Savannah, Georgia. DISTURBS requests that the Board not approve the applications due to the failure of Trust Company Bank of Savannah, Savannah, Georgia ("Savannah Bank"), a bank subsidiary of SunTrust, to meet the local credit needs of Savannah, Chatham County, Georgia.[3] SunTrust has met privately with DISTURBS on two occasions and has requested further meetings with the latter to discuss specific problems.

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[3] DISTURBS asserts that in Savannah, Georgia, SunTrust has failed to ascertain and meet the credit needs of low- and moderate-income neighborhoods and minority residents and has inadequately marketed credit services to same; has conducted inadequate small business lending efforts; has engaged in credit discrimination against women and minorities; and has inconvenient locations and hours of operation in low- and moderate-income neighborhoods.

In accordance with the Board's practice and procedure for handling protested applications,[4] the Board reviewed the allegations made by DISTURBS and SunTrust's response. The Board has also considered Savannah Bank's CRA record as detailed in its report of examination, as required by the CRA. In addition, SunTrust has indicated it will take a number of steps to enhance Savannah Bank's CRA performance. Savannah Bank will strengthen and expand consumer compliance by instituting more extensive training and review procedures for responsible personnel. The Bank will also strengthen its program to market credit services to minorities and low- and moderate-income neighborhoods, and its efforts to ascertain the credit needs of minorities and low- and moderate-income neighborhoods, through meetings with community representatives. Savannah Bank will also enhance its efforts to promote community development for minorities and low- and moderate-income neighborhoods by, among other things, engaging in discussions with representatives from the City of Savannah. SunTrust will file quarterly reports with the Federal Reserve Bank of Atlanta detailing SunTrust's progress in meeting its CRA objectives. Finally, SunTrust has also committed to strengthen consumer compliance in all of its banking subsidiaries.

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[4] See 12 C.F.R. § 262.25(c) (1987).

The Board has carefully reviewed the record of SunTrust in meeting the convenience and needs of the community of Savannah, Chatham County, Georgia. Based on this review and after taking into account SunTrust's commitments to enhance its service to meet the convenience and needs of all segments of the community, the Board concludes that convenience and needs considerations are consistent with approval of this application.[5]

Based on the foregoing and other facts of record, the Board has determined that the application under section 3 of the Act should be, and hereby is, approved. The acquisition of Commercial Bank shall not be consummated before the thirtieth calendar day following the effective date of this Order or later than three months after the effective date of the Order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of Atlanta, pursuant to delegated authority.

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[5] DISTURBS has also requested that the Board order a public meeting to receive public testimony on the issues presented by this application. Although section 3(b) of the Act does not require a formal hearing in this instance, the Board may order a formal or informal hearing. In the Board's view, the parties have had ample opportunity to present their arguments in writing and to respond to one another's submissions. Moreover, the Savannah Bank has requested additional meetings with Protestant to discuss specific problems. In light of these facts, SunTrust's proposals to expand its services, and other facts of record, the Board has determined that a hearing would serve no useful purpose. Accordingly, DISTURBS' request for a public hearing is hereby denied.

By order of the Board of Governors,[6] effective April 12, 1988.

James McAfee

James McAfee
Associate Secretary of the Board

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[6] Voting for the action: Chairman Greenspan and Governors Seger, Angell, Heller, and Kelley. Absent and not voting: Governor Johnson.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM

Gordon H. Mansfield

Q.1. As part of the Department of Housing and Urban Development (HUD) reform bill which Congress enacted late last year, I had a provision included to require mortgagee review boards to take action against Federal Housing Administration-participating lenders who illegally discriminate. What steps have been taken to implement this provision, to make sure that lenders who discriminate will not be able to do business with HUD?

A. A proposed rule to implement the changes in the Department of HUD Reform Act relating to the Mortgagee Review Board is currently in Department clearance. The Department expects to publish a proposed rule in August 1990. Meanwhile, the current HUD Mortgagee Review Board established by regulation, 24 CFR Part 25, has authority to take administrative actions, up to withdrawal of HUD/FHA approval of a mortgagee, for Fair Housing Act or ECOA violations. (See 24 CFR 25.9(o)).

Q.2. Since HUD's new authority became effective under the Fair Housing Act, how many complaints have you received for fair lending? What has been the disposition of those complaints to date?

A. In the period March 12, 1989 to April 24, 1990 HUD received 123 complaints of discrimination in lending. The Department has closed 113, with dispositions as follows: Thirty-five, no jurisdiction; thirty-two, administratively closed, (13 of these represent complaint withdrawals with some resolution); four were successfully conciliated; seven have been found by the Office of General Counsel not to demonstrate reasonable cause to believe that discrimination had occurred.

Ten complaints are still pending, six before the General Counsel and four in investigation.

Of the cases received by HUD but processed by FHAP agencies, thirty-three had determinations not to resolve (i.e., insufficient evidence of discrimination) and two were scheduled for administrative hearings.

Q.3. Describe in more detail the composition, activities, and decisions of the Fair Housing Task Force which your testimony mentioned.

A. The Fair Housing Task Force consists of senior officials from the Offices of Fair Housing and Equal Opportunity and Housing. The agenda of the group is to examine Housing/FHA single family operations to assure that they conform to the Fair Housing Act and that they affirmatively further fair housing. To date, the group has reviewed HUD Handbook 4155.3, Mortgage Credit Analysis for Mortgage Insurance on One-to Four-Family Properties, and agreed on several changes to assure conformity to the Fair Housing Act and Equal Credit Opportunity Act. These changes should be published this summer. A number of other handbooks relating to underwriting and appraisal are scheduled for review before the end of 1990. Also, copies of the Fair Housing Act and regulations will be included in "starter" kits for future applicants for mortgagee approval beginning later this summer.

Q.4. How will HUD monitor the mortgage bankers? What will HUD do with the new Home Mortgage Disclosure Act data?

A. HUD will be analyzing the data on mortgages granted by race and sex, and applicants rejected. If minorities and women are receiving unusually low rates of approval this may indicate possible discrimination. If minorities and women are receiving unusually high rates of approval this may also indicate discrimination through pre-screening which is preventing persons from filing applications. Institutions will then be examined more carefully, as appropriate, either by heightened monitoring or by conducting a Secretary-initiated investigation under the Fair Housing Act.

Q.5. HUD's testimony refers to its lack of enforcement authority under the Equal Credit Opportunity Act (ECOA). Given the overlap between the prohibitions of the Fair Housing Act and ECOA, is there anything to be gained by giving HUD such authority in fair lending cases involving mortgage discrimination?

A. Given the present coverage of the Fair Housing Act and the Equal Credit Opportunity Act, a complaint cognizable under both authorities could receive inconsistent dispositions at HUD and one of the Federal financial regulatory agencies. If HUD were to be given exclusive authority, such inconsistency could be avoided. The Fair Housing Act and HUD regulations already allow HUD to refer findings of Fair Housing Act violations by regulated businesses to the appropriate Federal, state or local governmental agency, with recommendations for appropriate disciplinary action. (24 CFR 104.935(a)).

Q.6. Has HUD yet issued the fair housing brochure, which it indicated would be issued this spring, to advise people of their rights under the Fair Housing Act?

A. The fair housing brochure is currently being printed and should be available to the public within 30-60 days. A copy of the brochure is attached.

Q.7. Testimony from the National Fair Housing Alliance recommended that HUD establish a Systemic Complaint Investigation Unit to focus on lending and insurance issues. What is your opinion of this proposal?

A. A unit already exists to handle systemic investigations: the Systemic and Secretary-Initiated Case Branch, in the Investigations Division, Office of Fair Housing Enforcement and Section 3 Compliance, in HUD Headquarters. Although the responsibilities of the unit extend beyond lending and insurance issues, HUD is developing guidance on those subjects and in-depth training will be conducted in FY 1991.

Q.8. In FIRREA Congress attempted to expand HMDA to all mortgage lenders (making more than five loans in a metropolitan statistical area). The Federal Reserve subsequently issued regulations saying that only mortgage bankers with more than $10 million in assets are required to keep HMDA data. Testimony from the Center for Community Change claims that these regulations exempt all but about three dozen mortgage companies from HMDA. Does HUD intend to use its regulatory authority to require the collection of HMDA data from a far larger number of mortgage bankers?

A. The amendments to the HMDA regulations recently promulgated by the Board of Governors of the Federal Reserve System limit the universe of mortgagees from which data will be collected to those having more than $10 million in assets and making or purchasing more than five loans in a metropolitan statistical area. However, HUD is now collecting, and has been for almost 20 years, racial and ethnic data on mortgagors and borrowers as well as their incomes and property locations, from all FHA mortgagees and Title I lenders, pursuant to authority conferred by the National Housing Act, section 311 of HMDA and the Fair Housing Act. Mortgagees have also been required to keep worksheets on all rejected applicants for mortgages and, in January of this year, HUD notified all direct endorsement mortgagees-responsible for over 90% of mortgages insured by HUD to send their worksheets for rejected mortgages to the Department. Direct endorsement mortgagees have been required to send the Department their worksheets on accepted applicants since the inception of the direct endorsement program.

The Department is now preparing a Mortgagee letter and a Title I letter, informing all FHA mortgagees and Title I lenders of the requirements of HMDA and the Federal Reserve Board's implementing regulations. These letters also will inform mortgagees and lenders that they will be required to report HMDA data to HUD, even if they report the same data to a Federal supervisory agency--one of which is HUD. Data submitted to HUD as an insurer, rather than as a HMDA Federal supervisory agency, cannot be forwarded to the Federal Reserve Board, but HUD will analyze basic data and make results available to the public. HUD will seek the necessary budget and other resources for the expanded data analysis and report functions.

Attached for information are copies of the January 1990 letter to direct endorsement mortgagees and an April 30, 1990 opinion from HUD's General Counsel, advising that HUD has the authority to collect HMDA data from all FHA mortgagees and Title I Lenders and to make such data publicly available.

Q.9. Describe the FHIP (Fair Housing Initiatives Program) and FHAP (Fair Housing Assistance Program) as they relate to mortgage discrimination, which your testimony mentioned.

A. FHAP

The Fair Housing Assistance Program (FHAP) provides funding to State and local fair housing enforcement agencies whose laws HUD has adjudged substantially equivalent to the Federal Fair Housing Act for the purpose of processing alleged Title VIII violations. One hundred twenty agencies receive funding for this activity.

Section 805 of the Fair Housing Act makes it unlawful for any person or business engaging in residential real estate-related transactions to discriminate because of race, color, religion, sex, handicap, familial status or national origin.

Residential real estate-related transactions include "the making or purchasing of loans or providing other financial assistance (1) for purchasing, constructing, improving, repairing, or maintaining a dwelling; or (2) secured by residential real estate."

State and local agencies receive $750 for each complaint processed which alleges a violation which is cognizable under the Fair Housing Act.

From 1981 to 1989 FHAP had a competitive Type II component that provided funds for innovative projects that addressed fair housing issues. The Kentucky Commission on Human Rights and The New York State Commission on Human Rights received a grant for a study that sought to document the extent of mortgage discrimination. This grant produced manuals for testers and test coordinators regarding tests for lending discrimination at the pre-application stage. In addition, the Kentucky Commission published reports based on HMDA data showing the volume of loans in Louisville and Lexington going to black and desegregated census tracts.

FHIP

The Fair Housing Initiatives Prpgram was established by section 561 of the Housing and Community Development Act of 1987 to strengthen the Department's efforts to enforce the Fair Housing Act. The program currently provides competitive funding to State and local governments, public or private nonprofit organizations and other public or private entities for education and outreach, and private enforcement.

HUD has just completed the first round of FHIP funding. The private enforcement initiative has funded a project proposed by a county fair housing center to study the extent and effect of mortgage discrimination on the residents of that county. The method to be used to ascertain this information will be the systematic testing of mortgage lenders using the HUD guidelines set forth in the FHIP regulation at 24 CFR Part 125.405. HUD expects to emphasize projects involving lending discrimination in future FHIP funding rounds.

U.S.DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON,D.C. 20410-8000

January 19, 1990

OFFICE OF THE ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

Direct Endorsement Letter 90-1

TO: ALL APPROVED DIRECT ENDORSEMENT MORTGAGEES

SUBJECT: Direct Endorsement Update - Sending Copies of Rejected Loan Applications to HUD

To further improve our internal control procedures, HUD will now require that all Direct Endorsement (DE) approved lenders submit to the local HUD Field Office a copy of the Form HUD 92900, Application for Commitment for Insurance and Form HUD 92900WS, Mortgage Credit Analysis Worksheet for all FHA applications rejected by DE underwriters. This requirement to send to the local office a copy of the Forms HUD 92900 and 92900WS for all rejected applicants is effective for all applications underwritten (worksheet signed by the DE underwriter) on or after March 18, 1990. (Please note that lenders may send either photocopies of the forms or send one of the tear-out copies.)

The local HUD Field Office will be entering certain data into our Computerized Home Underwriting Management System (CHUMS) from the HUD 92900 and HUD 92900WS. CHUMS will now track these rejects so that if the applicant requests a transfer of the case to another lender or submits a new application to another lender, HUD will be able to track the applicant and know that the applicant was previously rejected for mortgage insurance by a DE lender. This will improve our internal quality controls.

If you have any questions concerning this letter please contact the Headquarters Single Family Development Division at (202) 755-6700.

Very sincerely yours,

C. Austin Fitts
Assistant Secretary for Housing-
Federal Housing Commissioner

July 2, 1990

FAIR HOUSING

It's Your Right

THE FAIR HOUSING ACT

The Fair Housing Act prohibits discrimination in housing because of:

- Race or color
- National origin
- Religion
- Sex
- Familial status (including children under the age of 18 living with parents or legal custodians; pregnant women and people securing custody of children under 18)
- Handicap

WHAT HOUSING IS COVERED?

The Fair Housing Act covers most housing. In some circumstances, the Act exempts owner-occupied buildings with no more than four units, single-family housing sold or rented without the use of a broker and housing operated by organizations and private clubs that limit occupancy to members.

WHAT IS PROHIBITED?

In the Sale and Rental of Housing: No one may take any of the following actions based on race, color, national origin, religion, sex, familial status or handicap:

- Refuse to rent or sell housing
- Refuse to negotiate for housing
- Make housing unavailable
- Deny a dwelling
- Set different terms, conditions or privileges for sale or rental of a dwelling
- Provide different housing services or facilities

- Falsely deny that housing is available for inspection, sale or rental
- For profit, persuade owners to sell or rent (blockbusting) or
- Deny anyone access to or membership in a facility or service (such as a multiple listing service) related to the sale or rental of housing.

In Mortgage Lending: No one may take any of the following actions based on race, color, national origin, religion, sex, familial status or handicap:

- Refuse to make a mortgage loan
- Refuse to provide information regarding loans
- Impose different terms or conditions on a loan
- Discriminate in appraising property
- Refuse to purchase a loan or
- Set different terms or conditions for purchasing a loan.

In Addition: It is illegal for anyone to:

- Threaten, coerce, intimidate or interfere with anyone exercising a fair housing right or assisting others who exercise that right
- Advertise or make any statement that indicates a limitation or preference based on race, color, national origin, religion, sex, familial status or handicap. This prohibition against discriminatory advertising applies to single-family and owner-occupied housing that is otherwise exempt from the Fair Housing Act.

ADDITIONAL PROTECTION
IF YOU HAVE A DISABILITY

If you or someone associated with you:

- Have a physical or mental disability (including hearing, mobility and visual impairments, chronic alcoholism, chronic mental illness, AIDS, AIDS Related Complex and mental retardation) that substantially limits one or more major life activities
- Have a record of such a disability or
- Are regarded as having such a disability

your landlord may not:

- Refuse to let you make reasonable modifications to your dwelling or common use areas, at your expense, if necessary for the handicapped person to use the housing.

  (Where reasonable, the landlord may permit changes only if you agree to restore the property to its original condition when you move.)

- Refuse to make reasonable accommodations in rules, policies, practices or services if necessary for the handicapped person to use the housing.

  Example: A building with a "no pets" policy must allow a visually impaired tenant to keep a guide dog.

  Example: An apartment complex that offers tenants ample, unassigned parking must honor a request from a mobility-impaired tenant for a reserved space near her apartment, if necessary to assure that she can have access to her apartment.

However, housing need not be made available to a person who is a direct threat to the health or safety of others or who currently uses illegal drugs.

Requirements for New Buildings: In buildings that are ready for first occupancy after March 13, 1991, and have an elevator and four or more units:

- Public and common areas must be accessible to persons with disabilities
- Doors and hallways must be wide enough for wheelchairs

- All units must have:
  - An accessible route into and through the unit
  - Accessible light switches, electrical outlets, thermostats and other environmental controls
  - Reinforced bathroom walls to allow later installation of grab bars and
  - Kitchens and bathrooms that can be used by people in wheelchairs.

If a building with four or more units has no elevator and will be ready for first occupancy after March 13, 1991, these standards apply to ground floor units.

These requirements for new buildings do not replace any more stringent standards in State or local law.

HOUSING OPPORTUNITIES FOR FAMILIES

Unless a building or community qualifies as housing for older persons, it may not discriminate based on familial status. That is, it may not discriminate against families in which one or more children under 18 live with:

- A parent
- A person who has legal custody of the child or children or
- The designee of the parent or legal custodian, with the parent or custodian's written permission.

Familial status protection also applies to pregnant women and anyone securing legal custody of a child under 18.

Exemption: Housing for older persons is exempt from the prohibition against familial status discrimination if:

- The HUD Secretary has determined that it is specifically designed for and occupied by elderly persons under a Federal, State or local government program or
- It is occupied solely by persons who are 62 or older or
- It houses at least one person who is 55 or older in at least 80 percent of the occupied units; has significant services and facilities for older persons; and adheres to a published policy statement that demonstrates an intent to house persons who are 55 or older. The requirement for significant services and facilities is waived if providing them is not practicable and the housing is necessary to provide important housing opportunities for older persons.

A transition period permits residents on or before September 13, 1988 to continue living in the housing, regardless of their age, without interfering with the exemption.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410

OFFICE OF THE GENERAL COUNSEL

April 30, 1990

MEMORANDUM FOR: John C. Weicher, Assistant Secretary for Policy Development and Research, T

FROM: Frank Keating, G

SUBJECT: Expansion of Coverage of the Home Mortgage Disclosure Act

This responds to your memorandum of March 9, 1990, requesting our opinion as to the authority of HUD to collect and disclose information relating to FHA mortgage lending activities beyond the authority provided by the Home Mortgage Disclosure Act of 1975 (12 U.S.C. 2801, et seq.), as amended (hereinafter, HMDA). Section 309 of HMDA (12 U.S.C. 2808) and §203.3 of the implementing regulations promulgated by the Federal Reserve Board in 12 CFR Part 203, provide for the collection and disclosure of information about applicants and borrowers only with regard to mortgage lenders having assets in excess of $10 million. You have stated that the Offices of Housing, Fair Housing, and Policy Development and Research believe that it is important to "extend coverage of HMDA" to FHA mortgage lenders whose assets do not reach the $10 million threshold. We understand that to mean that the same kinds of information about applicants and borrowers should be collected and disclosed by HUD for all FHA mortgage lenders regardless of size, to the extent HUD has legal authority to do so.

It is our understanding that HUD collects the necessary information when loans are registered for insurance under Title I and mortgages are endorsed for insurance under Title II. We recently concurred on a proposed Mortgagee Letter which would require mortgagees to submit to HUD the application forms of rejected Title II applicants, and HUD has the authority to require similar submissions by Title I lenders if desired. The principal remaining issue pertains to authority to disclose the information received. We presume that any such disclosure, like the disclosure required under the Federal Reserve Board's HMDA regulations, would not disclose the characteristics of any individual applicant or borrower so that no personal privacy issues are involved.

HMDA §302(b) (12 U.S.C. 2801(b)) states that the purpose of the act is:

> [T]o provide the citizens and public officials of the United States with sufficient information to

> enable them to determine whether depository institutions are filling their obligations to serve the housing needs of the communities and neighborhoods in which they are located. . . .

The term "depository institutions" is defined in HMDA §303(2), and does not include most mortgage bankers. Therefore, as enacted in 1975, HMDA §302 did not cover the lending activities of many FHA mortgage lenders. However, HMDA §311 (12 U.S.C. 2810), which was added by §340 of the Housing and Community Development Act of 1980, states:

> Beginning with data for calendar year 1980, *the Secretary shall make publicly available data in the Secretary's possession for each mortgagee which is not otherwise subject to the requirements of this title* and which is not exempt pursuant to section 306(b) (and for each mortgagee making mortgage loans exempted under section 304(g)) with respect to mortgage loans approved by the Secretary for insurance under title I or II of the National Housing Act. Such data to be disclosed shall consist of data comparable to the data which would be disclosed if such mortgagee were subject to the requirements of section 304. Disclosure statements containing data for each such mortgagee for a primary metropolitan statistical area, metropolitan statistical area, or consolidated metropolitan statistical area that is not comprised of designated primary metropolitan statistical areas shall, at a minimum, be publicly available at the central depository of data established pursuant to section 304(f) for such primary metropolitan statistical area, metropolitan statistical area, or consolidated metropolitan statistical area that is not comprised of designated primary metropolitan statistical areas. The Secretary shall also compile and make publicly available aggregate data for such mortgagees by census tract, and tables indicating aggregate lending patterns, in a manner comparable to the information required to be made publicly available in accordance with section 310. (Underscoring ours)

The report of the Senate Banking, Housing, and Urban Affairs Committee (S. Rep. 96-736) states, in relevant part:

> Disclosure by HUD
>
> The bill provides that HUD shall make publicly available data in HUD's possession with respect to loans insured under Title I or II of the National Housing Act for mortgagees, such as mortgage bankers, which are not otherwise subject to the requirements of HMDA. HUD would also be required to compile and make publicly available aggregate data for such mortgagees by census tract, and tables indicating aggregate lending patterns, in a manner comparable to the information required to be made available by the Federal Financial Institutions Examination Council. (Underscoring ours)

Section 1211 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (Pub. L. 101-73) (hereinafter, FIRREA) expanded the coverage of HMDA in several respects: to include race, sex, and income of applicants and borrowers in the information to be collected and disclosed, and to cover all for-profit mortgage lenders not otherwise exempt. Thus, all mortgage bankers with assets over $10 million are now fully covered by HMDA. These newly-covered mortgage bankers are required to provide information to HUD. Except to the extent that insured loans are involved, Section 311 is not relevant and the $10 million asset test would apply to these mortgage bankers under HMDA even though they are reporting to HUD.

Section 311 applies to insured mortgage loans. It was amended by FIRREA only to extend the section's coverage to applications in addition to approved mortgage loans. It still applies to each mortgagee not otherwise covered by HMDA. The original principal objective of Section 311 may have been to include a type of lender--mortgage banker--otherwise exempt from HMDA. However, nothing in the wording of Section 311 suggests that the $10 million asset test was ever relevant for data collection and disclosure under Section 311. Now that mortgagee bankers as a class are not excluded from HMDA, the main remaining group of mortgage lenders excluded from the rest of HMDA but covered by Section 311 is comprised of all mortgage lenders with assets of $10 million or less. There is little point to Section 311 now unless it is read as covering the FHA activities of such mortgage lenders.

Accordingly, we believe that not only is the Secretary not precluded by HMDA from collecting and making public information concerning lending patterns for mortgagees and lenders whose assets are less than $10 million, but HMDA obligates the

Secretary to make any such information public if possessed by the Secretary.[1] The Federal Reserve Board regulation does not apply to these smaller mortgage lenders. However, HUD's obligation does not derive from that regulation; it is a statutory duty which cannot be relieved by regulation. HUD must carry out its duty outside the bounds of the Board regulation.[2]

The Secretary is also obligated to make this information available by §808(e) of the Fair Housing Act (42 U.S.C. 3608(e)), which states in relevant part:

> The Secretary of Housing and Urban Development shall--
>
> (1) make studies with respect to the nature and extent of discriminatory housing practices in representative communities . . . throughout the United States;
>
> (2) publish and disseminate reports, recommendations, and information derived from such studies, including an annual report to the Congress--

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[1] Pursuant to Section 306(b), the Federal Reserve Board regulations exempt from all HMDA requirements (including Section 311) any state-chartered or state-licensed financial institution subject to a state disclosure law substantially similar to HMDA, 12 CFR 203.3(b)(1). This minor exception is not important, given other HUD authority as discussed later in this memorandum.

[2] The Board has recognized that HUD may act to carry out Section 311 in areas not addressed by its regulation. For example, the preamble to the latest revision of the regulation, 54 F.R. 51360, indicates that prior to that revision HUD's collection of information on insured loans made by mortgage banking subsidiaries of bank and savings and loan holding companies (which are exempt from HMDA except as covered by Section 311) occurred entirely outside the regulation because HUD collection of information was not covered in the regulation. In fact, the Board's rulemaking to implement the 1980 HMDA amendments never mentions the new §311; see 46 F.R. 11780, February 10, 1981 (proposed rule) and 46 F.R. 40678, August 11, 1981 (final rule). The regulation now covers some HUD collection of information, but not all collection required by §311.

> (A) specifying the nature and extent of progress made nationally in eliminating discriminatory housing practices and furthering the purposes of this title, obstacles remaining to achieving equal housing opportunity, and recommendations for further legislative or executive action; and
>
> * * * * *
>
> (6) annually report to the Congress, and make available to the public, data on the race, color, religion, sex, national origin, age, handicap, and family characteristics of persons and households who are applicants for, participants in, or beneficiaries or potential beneficiaries of, programs administered by the Department. . . .

Another statutory provision that authorizes the Secretary to make this information public is §3(b) of the Department of Housing and Urban Development Act, which states that "The Secretary shall . . . conduct continuing comprehensive studies, and make available findings, with respect to the problems of housing and urban development."

The Freedom of Information Act (5 U.S.C. 552) (hereinafter, FOIA) would also authorize disclosure of information collected by HUD with regard to lending practices of lenders and mortgagees. The philosophy underlying this law favors public access to Government information. Ordinarily, this information would be provided after a request. But nothing in FOIA requires HUD to wait for a specific request for information, and the proposed disclosure of lending practices would be consistent with FOIA's underlying philosophy.

In conclusion, there is no legal obstacle to prevent HUD from publicly disclosing information it has received on the characteristics of FHA applicants and borrowers, regardless of the size of the lender, and HMDA requires this disclosure with respect to insured mortgage loans. The $10 million asset test in the Federal Reserve Board HMDA regulation does not apply to such mortgage loans. However, HMDA does not empower HUD or the Federal Reserve Board to require reporting on applicants or borrowers for uninsured mortgage loans from lenders who do not have more than $10 million in assets, and additional statutory authority would be needed for such a requirement.

IF YOU THINK YOUR RIGHTS ARE VIOLATED

HUD is ready to help with any problem of housing discrimination. If you think your rights have been violated, you may fill out the Housing Discrimination Complaint Form in this brochure, write HUD a letter or telephone the HUD Hotline. You have one year after an alleged violation to file a complaint with HUD, but you should file it as soon as possible.

What to Tell HUD:

- Your name and address
- The name and address of the person your complaint is against (the respondent)
- The address or other identification of the housing involved
- A short description of the alleged violation (the event that caused you to believe your rights were violated)
- The date(s) of the alleged violation

Where to Write: Send the Housing Discrimination Complaint Form or a letter to the HUD regional office nearest you (addresses on the Complaint Form) or to:

Office of Fair Housing and Equal Opportunity
U.S. Department of Housing and Urban Development
Washington, D.C. 20410-2000

Where to Call: If you wish, you may use the toll-free Hotline number: 1-800-424-8590. (In Washington, D.C., call 708-3500.)

If You are Disabled: HUD also provides:

- A toll-free TDD phone for the hearing impaired: 1-800-543-8294 (In Washington, D.C., call 708-2826.)
- Interpreters
- Tapes and braille materials
- Assistance in reading and completing forms

WHAT HAPPENS WHEN YOU FILE A COMPLAINT?

HUD will notify you when it receives your complaint. Normally, HUD also will:

- Notify the alleged violator of your complaint and permit that person to submit an answer
- Investigate your complaint and determine whether there is reasonable cause to believe the Fair Housing Act has been violated
- Notify you if it cannot complete an investigation within 100 days of receiving your complaint

Conciliation: HUD will try to reach an agreement with the person your complaint is against (the respondent). A conciliation agreement must protect both you and the public interest. If an agreement is signed, HUD will take no further action on your complaint. However, if HUD has reasonable cause to believe that a conciliation agreement is breached, HUD will recommend that the Attorney General file suit.

Complaint Referrals: If HUD has determined that your State or local agency has the same fair housing powers as HUD, HUD will refer your complaint to that agency for investigation and notify you of the referral. That agency must begin work on your complaint within 30 days or HUD may take it back.

WHAT IF YOU NEED HELP QUICKLY?

If you need immediate help to stop a serious problem that is being caused by a Fair Housing Act violation, HUD may be able to assist you as soon as you file a complaint. HUD may authorize the Attorney General to go to court to seek temporary or preliminary relief, pending the outcome of your complaint, if:

- Irreparable harm is likely to occur without HUD's intervention
- There is substantial evidence that a violation of the Fair Housing Act occurred

Example: A builder agrees to sell a house but, after learning the buyer is black, fails to keep the agreement. The buyer files a complaint with HUD. HUD may authorize the Attorney General to go to court to prevent a sale to any other buyer until HUD investigates the complaint.

WHAT HAPPENS AFTER A COMPLAINT INVESTIGATION?

If, after investigating your complaint, HUD finds reasonable cause to believe that discrimination occurred, it will inform you. Your case will be heard in an administrative hearing within 120 days, unless you or the respondent want the case to be heard in Federal district court. Either way, there is no cost to you.

The Administrative Hearing: If your case goes to an administrative hearing HUD attorneys will litigate the case on your behalf. You may intervene in the case and be represented by your own attorney if you wish. An Administrative Law Judge (ALJ) will consider evidence from you and the respondent. If the ALJ decides that discrimination occurred, the respondent can be ordered:

- To compensate you for actual damages, including humiliation, pain and suffering.
- To provide injunctive or other equitable relief, for example, to make the housing available to you.
- To pay the Federal Government a civil penalty to vindicate the public interest. The maximum penalties are $10,000 for a first violation and $50,000 for a third violation within seven years.
- To pay reasonable attorney's fees and costs.

Federal District Court: If you or the respondent choose to have your case decided in Federal district court, the Attorney General will file a suit and litigate it on your behalf. Like the ALJ, the District Court can order relief, and award actual damages, attorney's fees and costs. In addition, the court can award punitive damages.

IN ADDITION

You May File Suit: You may file suit, at your expense, in Federal District Court or State Court within two years of an alleged violation. If you cannot afford an attorney, the court may appoint one for you. You may bring suit even after filing a complaint, if you have not signed a conciliation agreement and an Administrative Law Judge has not started a hearing. A court may award actual and punitive damages and attorney's fees and costs.

Other Tools to Combat Housing Discrimination:

- If there is noncompliance with the order of an Administrative Law Judge, HUD may seek temporary relief, enforcement of the order or a restraining order in a United States Court of Appeals.
- The Attorney General may file a suit in Federal District Court if there is reasonable cause to believe a pattern or practice of housing discrimination is occurring.

For Further Information:

The purpose of this brochure is to summarize your right to fair housing. The Fair Housing Act and HUD's regulations contain more detail and technical information. If you need a copy of the law or regulations, contact the HUD regional office nearest you or:

Office of Fair Housing and Equal Opportunity
Room 5116
Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-2000
(202) 708-2878

Responses to Additional Questions for HUD

1. Please describe in some detail what data HUD is required to collect, what data it has been collecting, and what additional data HUD decided to collect this past October? Please include in your answer an explanation of the Computerized Housing Underwriting Mortgage System, the single family statistical system, and the Office of Policy Development and Research project, which were each referred to in HUD's section 1220 report.

HUD collects data on the application for insurance and the insurance process yielding information for management and underwriting purposes and also to measure workload. Such data include the name and address of the borrower or borrowers, property value, construction type (new or existing), type of borrower (owner occupied, investor), and type of transaction (purchase, refinance). This data collection process, which also yields operational data by State, field office, county, zip code and Census Tract, is collected through the Computerized Housing Underwriting and Management System (CHUMS).

The data in CHUMS are collected as part of the work process. CHUMS automatically performs routine and highly defined tasks, and was also designed to eliminate data transcription, reduce processing errors, shorten processing time, reduce costs and to impose uniformity of processing. CHUMS begins with the telephone call requesting an appraisal (application) and ends with the insurance endorsement, with the certificate of insurance being automatically produced.

The Consolidated Single Family Statistical System (CSFSS) begins with the creation of insurance records transported from CHUMS and ends with the termination of insurance and the ultimate disposition of property, if a claim is involved. All of the data in the CSFSS are extracted from other systems such as the default monitoring system, the property disposition system, the claims system and the insurance in-force system. Samples of case data are key punched from insured transactions covering specified data items on the structure from the appraisal forms and specific data on the borrower and the financial transaction from the mortgage credit application and its worksheet. The data are merged by FHA case number with the other data on the system and form a base to study borrower and loan transaction characteristics.

The data mentioned above have been collected historically. In October, it was determined that to be in conformance with HMDA, HUD should have additional information on rejected borrowers. Data screens were prepared and the necessary software was written and tested to gather information on the race, sex, income, the loan to value ratio, mortgage amount, sale price, mortgage payment/income ratio and expense/income ratio, address, Metropolitan areas, and Census Tract on rejected borrowers. A letter to All Approved Direct Endorsement Mortgagees was sent January 19, 1990 advising them of the new requirements effective March 18, 1990.

With respect to the Department's research agenda, HUD's Office of Policy Development & Research (PD&R) has developed a preliminary list of research themes and will complete the statement of work for a credit discrimination research conference by this summer. PD&R has also begun an analysis of FHA lending patterns for a small number of metropolitan areas in order to develop relevant measures of credit allocation by tract, race and income.

2. How has any of HUD's existing data been used to prosecute Fair Housing Act cases?

To date, HUD's reasonable cause determinations and prosecutions in administrative hearings under the Fair Housing Act have been based on information collected as a result of the investigation of individual cases rather than the information described in the answer to question number one.

3. HUD's testimony stated that the most effective way to detect discrimination is to gather the necessary data and to examine it for patterns of discrimination. What statistical information would prove or strongly suggest discrimination? Do you collect such information? If not, why not?

The Fair Housing Act states that the Secretary is to "determine based on the facts whether reasonable cause exists to believe that a discriminatory housing practice has occurred or is about to occur...." 42 U.S.C. 3610(g). HUD implementing regulations state:

> "... the General Counsel ... shall determine whether, based on the totality of the factual circumstances known at the time of the decision, reasonable cause exists to believe that a discriminatory housing practice has occurred or is about to occur. The reasonable cause determination will be based solely on the facts concerning the alleged discriminatory housing practice, provided by complainant and respondent and otherwise, disclosed during the investigation. In making the reasonable cause determination, the General Counsel shall consider whether the facts concerning the alleged discriminatory housing practice are sufficient to warrant the initiation of a civil action in Federal court." 24 CFR 103.400(a).

Accordingly, statistical information collected during an investigation may prove helpful in making a determination of whether reasonable cause has been established in any given case. The Department would consider such information, along with other evidence indicating that a complainant was treated differently than other similarly situated persons, in making its reasonable cause determination. Where a reasonable cause determination is made, the statistical information would be presented along with all other relevant evidence to an ALJ or, where any party elects to have a trial in Federal court, to a Federal District Judge.

4. Will the new statistical information to be gathered pursuant to the recently amended Home Mortgage Disclosure Act (HMDA) be sufficient to prove or strongly suggest discrimination (assuming disparities are present in the data)? Will this data be more useful than existing HMDA data? Will you use it in any way different from existing HMDA data?

The statistical information to be gathered under the new requirements of HMDA can suggest but not prove discrimination. However, the new information should be more useful than existing data on the location of loans issued. While it is difficult to say how good the data will be until we see them, information on the race, sex and income on rejected applicants should allow investigation in greater depth of specific locations or lenders. The data may help identify deficiencies that can be remedied or may show the need for additional information before discrimination or discriminatory practices can be confirmed.

5. Please comment on the changes in HUD's enforcement authority which have occurred as a result of the Fair Housing Act Amendments.

Prior to March 12, 1989 (the effective date of the Fair Housing Amendments Act of 1988), HUD had no enforcement authority. The Department's only powers under Title VIII of the Civil Rights Act of 1988 were to investigate complaints, determine whether to attempt to resolve them and, if so, attempt to conciliate them. In addition, HUD could refer pattern or practice cases, but not individual complaints, to the Department of Justice for its consideration in bringing a civil action.

The Amendments Act provides that HUD is to investigate and conciliate complaints concurrently. If a complaint is not conciliated, HUD (through its Office of General Counsel) determines whether there is reasonable cause to believe that a discriminatory practice has occurred. If so, Counsel issues a charge, which is adjudicated before an administrative law judge or, at the option of either party, in Federal District Court. The law judge may issue an order for appropriate relief, including actual damages, injunctive or other equitable relief and civil penalties. If the matter is heard in District Court, the Attorney General files the civil action and the District Judge may award actual and punitive damages, and other appropriate relief, including permanent or temporary injunction, temporary restraining order or other order including appropriate affirmative action.

The Secretary of HUD may also authorize the Attorney General to file a civil action for appropriate temporary or preliminary relief pending final disposition of a complaint filed with the Secretary.

6. In how many instances over the past three years has HUD found substantive violations of the Fair Housing Act or Equal Credit Opportunity Act (ECOA)? Provide some examples of how these substantive violations were resolved.

HUD does not make determinations of substantive violations under the Equal Credit Opportunity Act. Moreover, until March 12, 1989, HUD had no authority to enforce the Fair Housing Act. With the implementation of the Fair Housing Amendments Act of 1988, the Department was given the power to determine whether reasonable cause exists to believe that discriminatory practices have occurred and to initiate enforcement proceedings before an administrative law judge.

As of April 1, 1990, the Department found reasonable cause to believe that discriminatory housing practices occurred in 45 complaints. Twenty-two of these complaints are currently in administrative proceedings and 12 are in Federal District Court proceedings because a party has elected not to pursue the case in the administrative tribunal. The remaining cases were still in the 20 day election period.

As of May 11, 1990, one decision has been issued by a HUD ALJ under the amended Act. In The Secretary, United States Department of Housing and Urban Development, on behalf of Terry and Janella Herron v. Gordon G. Blackwell, HUDALJ No. 04-89-0520-1, the ALJ found that respondent Gordon G. Blackwell violated sections 804(a), (c), and (d) and 818 of the Fair Housing Act, and the regulations at 24 CFR sections 100.60(b)(2), 100.75(c)(1) and (2), 100.80(b)(1) and (5), and 100.400(c)(2). Mr. Blackwell, a white man, was found to have reneged on a contract to sell his house in Stone Mountain, Georgia, to a black couple, Terry and Janella Herron, for racially discriminatory reasons. Mr. Blackwell was ordered to proceed with the sale of the house to the Herrons according to the terms of the original contract and to pay damages in the amount of $44,591.60 (including $40,000 for embarrassment, humiliation and emotional distress) to the Herrons; $20,594.21 (including $20,000 for embarrassment, humiliation and emotional distress) to a couple who had moved into the house in question, ignorant of any controversy, after Blackwell has failed to honor his contract with the Herrons; and a civil penalty of $10,000 to the Department of Housing and Urban Development. The Secretary is currently seeking enforcement of this order before the Court of Appeals for the Eleventh Circuit.

7. How many fair lending written complaints did HUD receive over the past three years? How many of these complaints led to a finding of a substantive violation. Provide some examples of how these substantive violations were resolved.

HUD received fair lending complaints as follows:

Fiscal year 1988:		158
Fiscal year 1989:	10/1/88-3/12/89	61
	3/13/89-9/30-89	92
Fiscal year 1990:	10/1/89-4/24/90	31
Total:		342

These figures do not include cases HUD received which were subsequently processed by State or local agencies with laws equivalent to Title VIII.

As explained in the answer to question 5, HUD had no power to find substantive violations prior to March 12, 1989. Of the 342 complaints filed from October 1, 1987 to April 27, 1990, 155 were closed administratively, and HUD determined not to resolve 136. Of the remaining 51 complaints, 14 were conciliated successfully and 2 unsuccessfully; the remaining 35 complaints are pending.

Only one substantive violation has been found after an administrative hearing and that case, discussed in the answer to question 6, did not involve lending discrimination. There have, however, been a number of significant conciliations. For example:

- Three persons in a mid-West State alleged that their loan applications were rejected by a full service commercial bank based on national origin. The bank agreed to pay the complainants $27,900. In addition, under the Conciliation Agreement, the bank was required to (1) establish written screening criteria to be applied to all mortgage applications, (2) issue written notification of its nondiscrimination policy to all mortgage processors, (3) advertise as an Equal Housing Opportunity Lender, and (4) report to HUD (by HMDA loan register) for a 3 year period on the disposition of all loan requests.
- A complainant in a West Coast State alleged denial of a loan application by a savings and loan institution based on race (black). Under the terms of the Conciliation Agreement, the complainant received a loan of $150,000; further, the complainant could select the lower of two interest rates: (1) the rate available at the time of application, or (2) the rate available at the time of settlement.

8. How many fair lending telephone calls did HUD receive over the past three years? Can you characterize these inquiries? Are there any patterns among these inquiries? What are complainants told in response?

In the past 3 years, HUD Headquarters has received approximately 50 telephone inquiries regarding discrimination in lending. The typical call is from a person seeking a mortgage who has been asked by a lender to supply additional information. The callers indicate that they are told by the lender that there is additional information they must provide. They are reluctant to allege discrimination because they have not been denied the mortgage. However, they are unsuccessful in efforts to get the loan approved.

Callers are provided with appropriate guidance about the mortgage process in general and the coverage of the Fair Housing Act. Based on that information, if they wish to file a complaint, HUD receives their complaint over the telephone.

9. In how many instances over the past three years has HUD referred cases of possible discrimination to the Department of Justice for prosecution? What were the results?

HUD has no formal tabulation of cases referred to the Department of Justice during calendar years 1988 and 1989. However, based on a study of referrals made from 1981 through 1987, HUD estimates that approximately 20 cases are referred to DOJ annually. From March 1989 through April 1990 twenty-three cases were referred, including four complaints involving land use and zoning issues. Zoning complaints are required to be referred under section 810(g)(2)(C) of the Fair Housing Act.

The Department of Justice reported that it filed five suits in calendar years 1987 and 1988 based on HUD referrals. All were resolved by consent decree. Three were filed under the Fair Housing Act: United States v. Apollo Village, United States v. Atrium Village, and United States v. Allen and Kings Cove Condominium. Two were filed under Title VI of the Civil Rights Act of 1964 and the Fair Housing Act: United States v. Farmwell, North Carolina Housing Authority and United States v. Longbranch, New Jersey.

In addition, since March 12, 1989, the Attorney General has filed civil actions in 12 cases in which the Department of Housing and Urban Development made a determination of reasonable cause and an election was made to have the fair housing complaint adjudicated in Federal District Court.

10. Has HUD found violations of the Fair Housing Act or ECOA (Regulation B) based on an "effects test" analysis? Can you provide any specific examples of how you have used this approach to prohibit lenders from maintaining loan policies which have a discriminatory effect on minorities?

As noted in the answer to question 6, HUD does not make findings under ECOA.

As noted in response to questions 3 and 6, HUD determinations that reasonable cause exists to believe that a discriminatory housing practice has occurred have been based solely on the facts disclosed in the investigations of individual complaints.

11. Do appraisers, private mortgage insurers, or the secondary market play a role in discrimination? What should Congress do about the problem of under-appraisal of properties in minority areas? Would your agency detect this problem in its investigative or complaint-response procedures?

Appraisers, private mortgage insurers and the secondary market all play a vital role in providing mortgage financing; thus, their policies, procedures and practices are critical to ensuring non-discrimination in lending.

Both HUD and FNMA have put appraisers on notice as to their responsibilities. The uniform residential appraisal report states that "Race or the racial composition of the neighborhood are not considered reliable appraisal factors." In addition, fee appraisers appointed to field office appraiser panels must certify that they have read HUD's policy on neighborhoods. FNMA's appraisal guidelines are similar to HUD's.

With respect to the under-appraisal of property in minority neighborhoods, HUD has no systematic evidence about the existence or extent of under-appraisal. Such under-appraisal would constitute a violation of section 805 of the Fair Housing Act. Similarly, the discriminatory failure to provide private mortgage insurance and the discriminatory refusal to purchase loans would violate section 805.

HUD gathers information routinely by sampling appraisal reports on FHA-insured properties. This includes a desk review of 20 percent of all Direct Endorsement appraisals (95% of HUD business), and 100 percent of HUD processed appraisals (5% of business). A site visit is conducted for half of the appraisals that receive desk reviews. It is HUD's intention, over the next six months, to train HUD staff so they can identify any signs of discrimination in conducting desk reviews or site visits. In addition, use of the Secretary's power to initiate complaints, provided by the 1988 Fair Housing Amendments Act, should enable HUD, in time, to develop precedential cases which will alert the industry to prohibited conduct.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM
JOHN F. BOVENZI

FDIC
Federal Deposit Insurance Corporation
Washington, D.C. 20429

Office of Legislative Affairs

LA-7029

August 14, 1990

Honorable Alan J. Dixon
Chairman
Subcommittee on Consumer and
  Regulatory Affairs
Committee on Banking, Housing, and
  Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for your follow-up inquiry to our testimony of May 16, 1990 regarding discrimination in home mortgage lending.

Enclosed is our response. Please let us know if we can provide any additional information.

With best wishes.

Sincerely,

for
Beth L. Climo
Director

Enclosures

DIRECTOR HOPE
DIRECTOR, OLA
MS. MAHON
MS. GOUTHRO
MS. SMITH
MS. MCCORMICK
MR. ED MALAN (SBC)
MR. QUINCY
MS. GOODMAN
MS. MCINERNEY

FDIC RESPONSES TO FOLLOW-UP QUESTIONS
FROM SENATOR DIXON

1. In how many instances over the past three years has your agency found substantive violations involving mortgage race discrimination of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations? Explain how each of these substantive violations was resolved.

From January 1, 1987 through December 21, 1989, FDIC examiners found seven substantive violations involving mortgage race discrimination in FDIC-supervised institutions.

In three instances, we found that an institution's advertising excluded the required Fair Housing logo or the wording of advertisements implied discrimination. To correct the deficiencies, we required that the relevant advertising be revised.

In four instances, loan documents contained wording implying discrimination. To correct the problems, we required that the loan documents be revised to exclude such wording.

2. How many fair lending written complaints involving mortgage race discrimination did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation. Explain how each of these substantive violations was resolved.

From 1987 to the present, FDIC-supervised institutions were the subjects of nine written complaints involving mortgage race discrimination: one in 1987; one in 1988; four in 1989; and three so far in 1990. None of these complaints have led to a finding of a substantive violation involving mortgage race discrimination.

3. The Toledo Fair Housing Center received 102 mortgage discrimination complaints over the past 3 years just from the Toledo area -- of which about 40% showed probable cause. How many mortgage discrimination complaints did you receive for the entire U.S.? Is the number roughly proportional to the Toledo experience? If it is significantly lower, what factors might account for the difference?

As indicated in our response to your second question, the FDIC has received only nine written complaints involving mortgage race discrimination from 1987 to the present. In 1989, the FDIC also received one mortgage discrimination complaint based on the prohibited factor of age. Obviously, this is not proportional to the Toledo experience. There may be a variety of reasons for the disproportionate number of mortgage discrimination complaints received by the FDIC.

First, FDIC-regulated banks generally are the smaller to mid-sized institutions whose primary focus has not been directed toward providing mortgage credit. According to the 1988 HMDA aggregation reports (the most recent available), the institutions under the supervision of the following regulatory agencies originated the following percentages of home mortgage loans: the Office of the Thrift Supervision, 62%; the Office of the Comptroller of the Currency, 17%; the FDIC, 13%; the Federal Reserve Board, 7%; and the National Credit Union Administration, 2%. These reports do not reflect mortgage lending by other institutions such as independent mortgage or finance companies. Thus, while the Toledo Fair Housing Center probably receives mortgage discrimination complaints on the universe of mortgage lenders, the FDIC only receives them on state-chartered non-member banks.

Second, government regulatory authorities are sometimes viewed by consumers as having less credibility in policing discrimination than fair housing groups. In some cases, members of the public are fearful of filing a mortgage lending complaint against a local institution with a government regulatory agency. This is particularly so for residents of smaller towns. Even though FDIC staff explains to complainants that they are protected under the ECOA and Regulation B, as well as under the Fair Housing Act and its concomitant implementing regulations, callers are still sometimes reluctant to follow through with a written complaint. They may seek private counsel instead.

4. How many hours out of an examination will an examiner spend on fair lending enforcement? How many hours on the Community Reinvestment Act (CRA)? How often are these exams done?

The FDIC's Manual for Compliance Examinations provides instructions to examiners on how to examine for compliance with the fair lending laws. The following reflects average examination hours per institution spent on compliance examinations, the fair lending portion of the examination, and CRA from 1987 through 1989. Also presented are our examination frequency goals for compliance examinations and CRA examinations based upon an institution's compliance rating.

Average Examination Hours

	1987	1988	1989
Compliance (Total)	51	55	57
CRA	5	5.5	7
Other Fair Lending	8.5	9	9

(NOTE: Average hours may vary due to the size of an institution. For institutions with less than $50 million in assets to those with assets of over $500 million, the ranges were: 42-139 hours in 1987; 44-142 hours in 1988; and 43-167 hours in 1989. These figures do not include hours spent on compliance visitations, which often include a review of compliance with fair lending laws.)

Examination Frequency Goals

Compliance Rating	Maximum Interval (in months)
1	24
2	24
3	24
4	12
5	12

CRA Rating	Maximum Interval
Outstanding	24
Satisfactory	24
Needs to Improve	12
Substantial Noncompliance	12

5. In your exams, do you check whether certain minority neighborhoods have higher rejection rates than comparable white neighborhoods?

FDIC examination procedures include methodologies to compare rejection rates by location and race. The attached FDIC logsheets have been the primary tool used by examiners to compare the treatment of applicants based on race and location. However, the census tract designations are not included on the logsheet but must be accessed from individual loan applicants. This is a very time consuming process, and where resources have been limited, this was not always done.

The FDIC expects the current compliance examination procedures to be modified to reflect the new HMDA data that will be collected as a result of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. The HMDA data, expected to be available in late 1991, is expected to far exceed the usefulness of the logsheet by providing cross-tabulated totals of home applicants accepted and rejected by the race, gender and income of applicants, as well as by census tract characteristics of the properties for which loans are sought. In the future, we anticipate that FDIC examiners will be able to check minority rejection rates by neighborhood relative to nonminorities because of the improved data reporting.

6. What are your examiners trained to do when they find a lending institution with a policy of requiring a minimum loan size, lot size or income level? a maximum age of the house? that the neighborhood was stable or improving? How many institutions have been cited for this?

The FDIC Manual for Compliance Examinations (Fair Housing section), contains policy guidance that addresses the so-called "effects test", i.e., policies or practices that appear neutral on their face, but which result in the rejection of a higher proportion of credit applications received from members of a protected group. FDIC examiners must cite in an examination report any possible "effects test" violations and any "business necessity" justifications offered by an institution. If the latter are not offered or such a need is not effectively established, examiners generally recommend a policy change to the institution.

The FDIC compliance examination data base does not track "effects test" violations per se. Instead, it tracks the subject of the violation. Consequently, we do not have data on the number of institutions cited for "effects test" violations. The following are two examples of situations in which examiners found "effects test" problems during an examination and required the institutions to make changes to correct the problems.

In one case, a bank's written loan policies stated that the bank would make mortgage loans only to individuals with a minimum income of $800 per month. Moreover, the income of a co-applicant would not be taken into account in determining the minimum income amount. This same bank's written loan policies indicated that mortgage loans would be made only for homes with a minimum of 900 square feet. Finally, the policies required that at least a three percent real estate commission be paid in connection with a property for which the institution would be making a mortgage loan.

To correct these problems, the examiner pointed out the possible discriminatory effects of these policies and required the bank to change its written loan policies.

In another case, a bank's written loan policies (and the practice followed by bank employees) required that mortgage loans on nonapproved Federal Home Loan Mortgage Corporation and Federal National Mortgage Association dwellings would be made only if the borrower made a down payment of at least 25 percent of the appraised value of the property. The bank's trade area was inhabited predominately by Hispanics. Other financial institutions in the immediate area, all of which were savings and loan associations, required the normal 20 percent investment on the part of the borrower.

In this case, the policy was not changed during the examination. However, the examiners indicated that the matter would be reviewed by the institution's management. Our follow-up to the examination found that the situation was reviewed by bank management and appropriate policy changes were instituted.

7. If a loan were denied because of a low appraisal on the property -- as is often the case in minority neighborhoods -- will the examiner check this in its computerized sampling technique? Will the examiner be able to check whether the appraisal itself was based on illegal discrimination?

The FDIC uses no computerized sampling technique in examining for compliance with fair lending laws. However, the examination procedures set forth in the Manual for Compliance Examinations contain instructions for examiners to review a sample of rejected home loan applications with particular emphasis on applications from minorities. Examiners are then directed to determine whether the information available in the records is consistent with and supports the reasons for denial stated in the adverse action notices. Examiners must also determine whether the reasons for rejection are consistent with the institution's lending policies, and that these policies were applied consistently to both minority and nonminority applicants. In addition, illegal discrimination based on the appraisal process may be discovered during the examination process. The examiner is responsible for checking to see whether the appraisal itself was discriminatory in nature.

8. Some regulatory agencies have testified that their examination techniques test for discriminatory practices by comparing rates of one financial institution with others in the same area. Do wide disparities exist between institutions? Give some examples (without revealing names). Various aggregate studies imply that lenders across the board may be discriminating. Would not this technique then suggest that no problem exists, when in fact there is a major problem?

FDIC examiners use the aggregate HMDA reports currently available, which show the total number of loans made in individual census tracts by all lenders in a Metropolitan Statistical Area (MSA), as a broad measure for comparing the loan activity of the institution being examined against that of its peers in the same MSA. When a high degree of difference between the loan activity of any individual institution and that of its peers is evidenced by the aggregate reports, examiners will obtain from the Washington Office the individual HMDA statements filed by competing institutions. As a measure of loan demand based on loan originations, examiners can see from both the aggregate data and the statement filed by peer institutions whether loans are being made by other lenders in certain census tracts, but not by the institution being examined.

Based on our review of available data, there do not generally appear to be wide disparities among institutions lending in the same area. However, our data also indicate that there is not widespread evidence of discriminatory practices among the institutions we supervise.

9. No agency has referred cases of possible discrimination to the Department of Justice for prosecution. Have you referred any cases to the Department of Housing and Urban Development (HUD)?

Since 1977, the FDIC has referred a few complaints to HUD pursuant to the "Memorandum of Understanding Regarding Interchange of Information Concerning Complaints Involving Discrimination in Financing" (attached). With more data being generated, discussions with HUD representatives are underway regarding the possibility of updating this agreement.

10. HUD testified last October that the most effective way to detect discrimination is to gather the necessary data and to examine it for patterns of discrimination. What statistical information would prove or strongly suggest discrimination? Do you collect such information? If not, why not?

The FDIC Manual for Compliance Examinations directs FDIC examiners to gather specified data and to examine it for patterns of discrimination. Our examination procedures with regard to discovery of possible illegal discrimination are premised on the process of comparison, using a control group and a comparative group. Examiners select files based on the presence of the characteristics being used as a litmus and compare them with a control group (e.g., minority married couples vs. white married couples). Examiners are required to perform even more in-depth probing, if, for example, the statistical information reveals that the percentage of rejected minority or female applicants "significantly exceeds" the percentage of rejected control group applicants.

When statistics indicate a possible problem area, examiners are then required to investigate the underlying reasons. The FDIC believes the examination procedures now in use are adequate relative to the collection of and use of statistical information. (See also the answer to Question 11.)

11. Will the new statistical information to be gathered pursuant to the recently amended Home Mortgage Disclosure Act (HMDA) be sufficient to strongly suggest discrimination (assuming disparities are present in the data)? Will this data be more useful than existing HMDA data? Will you use it in any way different from existing HMDA data?

The FDIC believes that the new statistical information to be gathered pursuant to the recently amended HMDA will be an improvement over data currently available. The aggregate tables of information will result in evidence adequate to raise a presumption of discrimination, or lack of discrimination, unless refuted. Such evidence is currently available only after considerable research on the part of experienced examiners. We expect to use the data as a vehicle for improved enforcement of the Community Reinvestment Act. Of particular assistance will be those tables containing comprehensive totals concerning the disposition and treatment of applications received from low- to moderate-income minority applicants, as compared to those from nonminority applicants. In general, because of the improved presentation of HMDA information, we expect to be able to develop improved insight into an institution's lending patterns, and thus be able to question an institution's management concerning its patterns of lending to particular neighborhoods. The HMDA information will be even more useful when the new 1990 Bureau of the Census data becomes available.

12. The Center for Community Change has recommended in its testimony that each regulatory agency should adopt regulations similar to the Office of Thrift Supervision's (OTS) nondiscrimination regulation, which prohibits redlining and requires written loan policies to be made publicly available. The OTS believes that requiring all savings associations to make available to potential borrowers their clear, nondiscriminatory loan underwriting standards is an important safeguard to assure uniform application. What do you think of this idea?

The FDIC has given consideration to adopting such a regulation. However, we believe that adequate regulations and procedures are in place to ensure enforcement of the nondiscrimination laws. The redlining and other practices prohibited under the OTS regulation are already illegal under Federal law. The FDIC requires banks to adopt policies and procedures to carry out these anti-discrimination laws. Also, we do not believe that making loan policies publicly available will be an effective way to prevent mortgage discrimination. In order to identify and stop discriminatory practices, one must look at how a bank implements its written loan policies. Merely reviewing a bank's written loan policy is not likely to reveal evidence of discrimination.

13. The National Fair Housing Alliance recommended in its testimony at both hearings that a brochure for mortgage loan applicants explaining how to recognize subtle acts of discrimination and how to file complaints be provided to every loan applicant who is rejected. Most of the regulatory agencies have indicated that new brochures for consumers would be useful. How much input will the agencies be getting from civil rights specialists in designing these brochures? How will they be different from past brochures? When will they be distributed and how? Will the brochures include phone numbers for the Justice Department's Civil Rights Division, HUD's Fair Housing and Equal Opportunity Division, and local public or private fair housing agencies?

We have not yet made a decision on whether or not to publish a new brochure for mortgage loan applicants. However, we anticipate that any such brochure would be developed on an interagency basis, with significant input from staff knowledgeable about civil rights and fair lending issues. A listing of appropriate federal agencies to contact would probably be included, as is done in other consumer information brochures issued by the FDIC and FFIEC.

The FFIEC's Citizen's Guide to CRA, which includes information on how to file a complaint, is currently being updated to reflect the FIRREA's amendments to the CRA.

The FDIC also participates in the publication of the U.S. Office of Consumer Affairs Consumer's Resource Handbook (attached). This publication includes guidance on how to write a complaint letter and provides an extensive directory of federal, state, and local agencies and other offices that can be contacted for assistance.

14. The testimony from the Western Center on Law and Poverty charges that the FDIC did not properly handle a CRA complaint by the Committee for Accountable Reinvestment. According to the testimony, the FDIC's Los Angeles area staff initially refused to meet with Committee representatives and refused to allow staff of elected local officials to attend the meeting. Please explain relevant FDIC policies for handling CRA complaints. Do you believe the FDIC's response was appropriate?

FDIC policy provides for examiners to make outside contacts in conjunction with compliance examinations when necessary to assess an institution's performance in meeting community credit needs under the CRA. With respect to the above example, we believe the FDIC's response was appropriate.

Examining personnel in our San Francisco Region scheduled meetings with representatives of the Committee for Accountable Reinvestment (CAR) and several other community groups in conjunction with a regularly scheduled examination of Mitsui Manufacturers Bank (MMB), Los Angeles, California. Because of comments regarding the CRA performance of MMB submitted to the Federal Reserve Board in connection with the application by the Mitsui Bank, Limited (MMB's parent) and the Taiyo Kobe Bank, Limited to acquire Taiyo Kobe Bank and Trust Company in New York, our examiners made an extra effort to meet with concerned groups. The FDIC had not and did not receive a complaint against MMB from any of the groups.

To facilitate the order and effectiveness of meetings, and often because of space restrictions, it is necessary to limit attendance to principal spokespersons of a community or group. The initial request to meet by CAR involved a rather large number of individuals, including not only CAR members but staff of certain local elected officials not members of the group. We decided to limit the number of participants and prohibit elected officials or their staffs from attending to ensure an orderly and productive meeting and to keep the meetings from being unduly politicized. The resulting meetings with all concerned groups, including CAR, brought forth views that were taken into account in our examination of the institution.

15. Are the FDIC's fair lending examination techniques the same as those of the Federal Reserve? The Federal Reserve claims to send out consumer examiners with laptop computers to do analyses of comparable accepted and rejected loan applications.

Examination procedures for fair lending, as well as most other consumer protection laws and regulations, are developed by the FFIEC Consumer Compliance Task Force. Thus, the procedures are uniform among the participating regulatory agencies. The actual implementation of the procedures and techniques used may vary because of organizational and other differences among the agencies. In examining for compliance with the fair lending laws, FDIC examiners include analyses of accepted and rejected loan applications, although there is no required or standardized use of laptop computers in this activity.

MEMORANDUM OF UNDERSTANDING REGARDING INTERCHANGE OF INFORMATION CONCERNING COMPLAINTS INVOLVING DISCRIMINATION IN FINANCING

The Department of Housing and Urban Development, the Department of Justice, and the four principal Federal Financial Regulatory Agencies (the Comptroller of the Currency, the Federal Home Loan Bank Board, the Federal Reserve Board and the Federal Deposit Insurance Corporation) agree to the following exchange of information concerning complaints of discrimination in financing.

I. The Department of Housing and Urban Development

A. HUD will provide the appropriate Federal Financial Regulatory Agency with a copy of all complaints received pertaining to discrimination in financing that have been accepted for investigation.

B. HUD will provide a copy of the notice to resolve or not to resolve served on the respondent to the appropriate Federal Financial Regulatory Agency.

C. The Department of HUD will provide the Department of Justice a monthly listing of financial institutions against whom complaints have been filed.

D. In appropriate instances, where there is a failure to conciliate, the Department of HUD will refer such cases to the Department of Justice for its consideration for action under Section 805.

E. HUD will provide a copy to the appropriate Federal Financial Regulatory Agency of the notification to Justice when HUD's attempts to conciliate a complaint have failed.

II. The Federal Financial Regulatory Agencies

A. Each Federal Financial Regulatory Agency will provide HUD with a copy of all complaints received by the Agency pertaining to discrimination in financing together with an indication of action taken or contemplated by the Agency on the complaint.

FDIC
Federal Deposit Insurance Corporation
Washington, DC 20429

Division of Bank Supervision

FAIR HOUSING

BL-12-88
March 28, 1988

TO: CHIEF EXECUTIVE OFFICERS OF
INSURED STATE NONMEMBER BANKS

SUBJECT: Fair Housing Lending Home Loan Application Log Sheet

The Office of Management and Budget (OMB) has approved for continued use the attached camera-ready Home Loan Application Log Sheet. Reproduction of the log sheet is the responsibility of each institution required to maintain this record under Part 338, FDIC Fair Housing Regulations.

This form is the same as that distributed with BL-51-1985, dated December 31, 1985, except that the OMB expiration date has been extended from April 30, 1988 to September 30, 1990. The printing date of this form is March, 1988.

Questions concerning the fair housing regulations or enforcement program should be directed to your FDIC Regional Office.

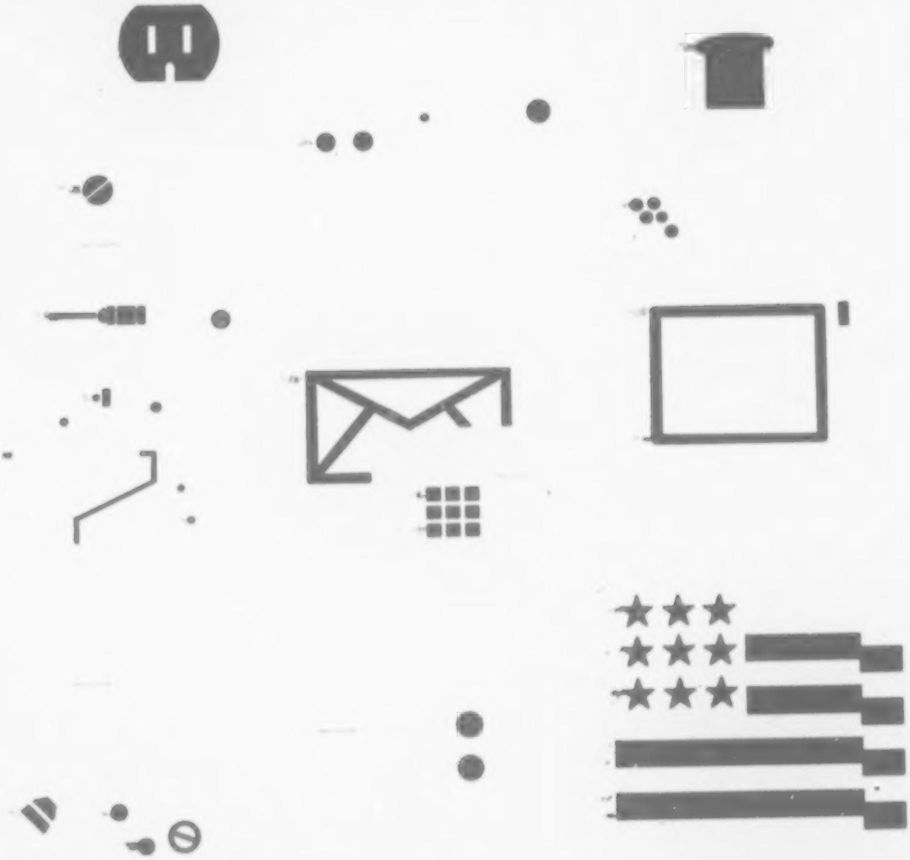
Paul G. Fritts
Director

Enclosure

Distribution: Insured State Nonmember Banks (Commercial and Mutual)

Consumer's

RESOURCE HANDBOOK



Office of the Special Adviser to the President for Consumer Affairs
The White House, Washington, DC
and the
United States Office of Consumer Affairs

in cooperation with the
Federal Deposit Insurance Corporation

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM
JERAULD C. KLUCKMAN

1989

Office of Thrift Supervision
Department of the Treasury
1700 G Street, N.W., Washington, D.C. 20552

July 27, 1990

Senator Alan J. Dixon
Chairman, Subcommittee on Consumer
and Regulatory Affairs
United States Senate Committee on
Banking, Housing, and Urban Affairs
Washington, D.C. 20510-6075

Dear Senator Dixon:

This is in response to your letter of June 12, 1990, asking for our answers to several questions relating to our testimony at your Subcommittee's May hearings on mortgage discrimination.

Q.1. In how many instances over the past three years has your agency found substantive violations involving mortgage race discrimination of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations? Explain how each of these substantive violations was resolved.

A.1. As explained in our testimony, the Office of Thrift Supervision (OTS) considers substantive violations to include those constituting evidence of overt discrimination, differential treatment of loan applicants on a prohibited basis, making significant errors with respect to maintaining a loan application register, not using the Equal Housing Lender logotype in advertisements, or failing to furnish adverse action notifications. We also indicated in our testimony that we are in the process of developing a data base of examination statistics and cited violations to help us more accurately monitor the extent of compliance by savings institutions.

In response to your question, we have evaluated the available data regarding the twelve savings associations which we testified have been cited for substantive violations over the past three years (1987 - 1989). The majority of the substantive violations involved citations of adverse action notification requirements, with the remaining violations involving citations of record retention requirements or monitoring information requirements. Based on the available data, we cannot determine if any of these violations specifically involved mortgage race discrimination. It is possible that the violations regarding monitoring information could have mortgage race discrimination implications, but that cannot be affirmatively determined.

Violations of law or regulation are included in reports of examination and communicated to a savings association's management. The report is transmitted to the association by way of a supervisory letter that instructs the association's management to institute corrective measures. Violations are typically resolved through interaction with senior management. Our answer to question 15 contains additional information on the supervisory process.

Q.2. How many fair lending written complaints involving mortgage race discrimination did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation? Explain how each of these substantive violations was resolved.

A.2. Our automated consumer complaint system indicates that over the past three years (1987-1989), the agency received two complaints coded as allegations of mortgage race discrimination, that resulted in some finding of regulatory violation.

- In the first case, a special limited examination was conducted, but the examination found no evidence of discrimination. However, the savings association was cited for serious deficiencies in recordkeeping, and instructed to establish corrective procedures.

- In the second case, district staff determined no discrimination had occurred because the applicants' combined debt to income ratio was far above the savings association's standards, as well as customary industry requirements. However, the association was cited for using an outdated and incomplete ECOA statement, and was required to revise its documents.

Q.3. The Toledo Fair Housing Center received 102 mortgage discrimination complaints over the past 3 years just from the Toledo area -- of which about 40% showed probable cause. How many mortgage discrimination complaints did you receive for the entire U.S.? Is the number roughly proportional to the Toledo experience? If it is significantly lower, what factors might account for the difference?

A.3. Over the past three years, this agency has received approximately 360 complaints of mortgage discrimination nationwide as compared to the 102 received by the Toledo Fair Housing Center. We have no basis for determining whether the center's experience is proportional to ours. This agency only handles complaints directed at OTS-regulated savings associations; the Toledo Fair Housing Center's number of 102 complaints is probably comprised of complaints directed at many types of financial institutions, including mortgage companies and finance companies. These entities are not subject to routine examinations or to regulations as strict as those that apply to savings associations.

The complaint volume experienced by the Toledo Fair Housing Center may be due to its visibility and accessibility to local residents. We have taken steps, and will be taking additional measure to make the general public more aware of our responsibilities in this area. For example, we have already taken actions to participate in regional HUD public education panels, and to provide the revised FFIEC booklet on Consumer Rights to a broad-based list of community and civil rights organizations. We are also developing a news release on our complaint procedures.

Q.4. How many hours out of an examination will an examiner spend on fair lending enforcement? How many hours on the Community Reinvestment Act (CRA)? How often are these exams done?

A.4. As explained in our answer to question number 1, the OTS does not yet have a fully operational data reporting system for our separate compliance examinations. Consequently, in order to answer this question, we pulled a random sample of recent compliance examination reports from five of our Districts and performed some manual tabulation.

Based on the sample, OTS examiners spent, on average, 19.3 hours on-site performing the fair lending portion of the compliance examination. The term "fair lending" refers to the Equal Credit Opportunity Act, OTS Nondiscrimination Regulations, Fair Housing Act, and Home Mortgage Disclosure Act. Average on-site time for CRA was 14.8 hours. The total for the two areas addressed in your inquiry was 34.1 hours on-site per examination. The average total on-site time for the examinations in the sample was 82.1 hours. The average asset size for the sample was $120 million.

On a percentage basis, 23.5 percent of the on-site time is spent on fair lending and 18 percent is spent on CRA. Combined, these two areas comprise 41.5 percent of our on-site compliance examination hours.

Our compliance examination frequency is driven by the lower of the compliance or CRA rating assigned at the previous examination. The compliance rating system employs a "1" to "5" scale with "1" being the highest and "5" being the lowest rating. The CRA rating system is the new, four-tiered descriptive system which went into effect on July 1, 1990 pursuant to FIRREA. Savings associations rated "1" and "2" for compliance or "outstanding" and "satisfactory" for CRA receive compliance examinations on a 24 month cycle. Savings associations rated "3" and "4" for compliance or "needs to improve" for CRA receive compliance examinations on a 12 month cycle, and those rated "5" for compliance or "substantial noncompliance" for CRA receive compliance examinations on at least a 6 month cycle. Our Districts have the flexibility of conducting compliance examinations on shorter cycles than those discussed above, or supplement regular examinations with targeted visits should circumstances warrant.

Q.5. In your exams, do you check whether certain minority neighborhoods have higher rejection rates than comparable white neighborhoods?

A.5. In performing our Nondiscrimination and Fair Housing Act examination procedures, OTS examiners make use of reports from our Loan Application Register/Data Submission Report system. These reports analyze a given savings association's lending patterns using six-month reporting cycles. Output reports from this system are available on a national, OTS District, Metropolitan Statistical Area, and individual savings association levels. The output reports indicate, by raw number and percentage, data regarding the total number of mortgage loan applications received, granted, rejected or denied, withdrawn, and pending in each cycle. (Identical reports are also prepared for home improvement and mobile home loans). The data is further separated into four different reporting categories: census tracts; race; sex; and, marital status. Our previous written statements to the Subcommittee have explained these reports in some detail.

With this in mind, the answer to your question is in the affirmative if you consider the term "neighborhoods" to be substantially similar to the term "census tracts." Our examiners are able to use the LAR/DSR output reports to spot disparities in lending patterns with regard to census tracts with various characteristics. The census tract data portion of a LAR/DSR output report is broken down into several categories: both low income and substantially minority; both moderate income and substantially minority; low income but not substantially minority; moderate income but not substantially minority; not low or moderate income but substantially minority; all other tracts; and, non-tracted areas. Therefore, examiners are able to compare acceptance and rejection rates between substantially minority and non-minority census tracts.

Q.6. What are your examiners trained to do when they find a lending institution with a policy of requiring a minimum loan size, lot size or income level? a maximum age of the house? that the neighborhood was stable or improving? How many institutions have been cited for this?

A.6. As part of the OTS nondiscrimination examination process, the examiner reviews all lending practices and policies of a savings association. If a lending practice or policy such as a minimum loan size or income level is identified, the examiner reviews whether the policy has a disproportionate impact on any prohibited basis, type of census tract, or property age group.

This review entails the following: (1) the examiner determines if applications reflect illegal prescreening or other factors which would limit the inflow of applications from any protected group; (2) the examiner determines if the savings association rejects applications from any group with a disproportionate frequency or if its acceptance levels are disproportionately lower for one or more groups; (3) the examiner determines whether any discrepancies between groups are large enough to warrant further study.

Assuming there are such discrepancies, the examiner tests any hypothesis raised during the steps performed above through a review of a representative sample of loan or application files. Lending policies are also evaluated in light of the "effects test" under Regulation B (12 CFR 202.6(a)) and OTS regulations (12 CFR 528.2(a) and 571.24(b)) for items such as underwriting standards which appear to have no economic basis. After an evaluation of the reasons for the discrepancies by the examiner, if the savings association cannot rebut the presumption of less favorable treatment as demonstrated by the association's files, the examiner will appropriately report a finding of discrimination.

Savings associations are prohibited by OTS regulations from refusing to lend or lending on less favorable terms in a particular area because of the racial composition of the area (see 12 CFR 571.24(c)(6)). Refusing to lend, or offering less favorable terms to applicants because of the income level in an area is also prohibited as it can have the effect of discriminating against minorities.

Moreover, savings associations are prohibited from denying a loan or other service on the basis of the age or location of a dwelling and from discouraging or refusing to consider any application based on the age or location of a dwelling (see 12 CFR 528.2(a) and 571.24(c)(7)). A savings association is also prohibited from relying on an appraisal of a dwelling which it knows, or reasonably should know, is discriminatory on the basis of the age or location of a dwelling, or is discriminatory per se or in effect under the Fair Housing Act or the Equal Credit Opportunity Act.

Minimum loan size policies are also addressed by OTS regulations (12 CFR 528.2(a)). No savings association may discriminate on a prohibited basis in fixing the amount (e.g. minimum loan size), of a loan or other service. While OTS regulations do not prohibit savings associations from setting minimum loan sizes, it is clear that such policies must not be discriminatory or have a discriminatory effect on a prohibited basis.

Violations of the above-mentioned nondiscrimination requirements and the impact of policies such as those addressed in your question are also taken into consideration as part of a savings association's assessment under the Community Reinvestment Act.

At this point, we do not have an operational data system that would indicate how many savings associations were cited for these violations.

Q.7. If a loan were denied because of a low appraisal on the property -- as is often the case in minority neighborhoods -- will the examiner check this in its computerized sampling technique? Will the examiner be able to check whether the appraisal itself was based on illegal discrimination?

A.7. OTS compliance examiners review loan application registers and data submission reports for discrepancies based on applicant and property characteristics as part of the nondiscrimination portion of the compliance examination. When discrepancies are apparent, a judgmental sample of files is selected for review. Part of this process requires the examiner to make a determination as to whether the savings association's lending patterns for the affected group(s) reflect appraisals which are substantially lower than the purchase price or requested loan amount. If patterns of "low-balling" regarding protected groups, geographic areas and older properties are found in the sample, the practice and its effect is included in the examination report. The issue of excessively low appraisals is addressed as part of the examination objectives for compliance with the OTS nondiscrimination regulations.

Q.8. Some regulatory agencies have testified that their examination techniques test for discriminatory practices by comparing rates of one financial institution with others in the same area. Do wide disparities exist between institutions? Give some examples (without revealing names). Various aggregate studies imply that lenders across the board may be discriminating. Would not this technique then suggest that no problem exists, when in fact there is a major problem?

A.8. We are reading your reference to the term "rates" to mean mortgage loan acceptance or rejection rates as opposed to interest rates. One of our nondiscrimination examination procedures includes a step requiring a comparison of the subject savings association's lending data with that of others in the area. The purpose of the comparison is to help the examiner gain a better understanding about factors such as loan demand, market share, and application patterns in the area. There is no "norm" or benchmark for measurement of acceptance or rejection statistics between lenders in the same area. We would certainly agree that this type of comparison is seriously flawed if it is being contrived to buttress the shallow notion that no discrimination has occurred if all local lenders' statistics are comparable. We would also suggest that the same illogic prevails when a conclusion regarding discriminatory treatment is reached when the comparison shows that the subject institution's rejection ratios are higher than those of other local lenders.

Q.9. No agency has referred cases of possible discrimination to the Department of Justice for prosecution. Have you referred any cases to the Department of Housing and Urban Development (HUD)?

A.9. Prior to March 12, 1989 (the effective date of the Fair Housing Amendments Act), this agency initiated consultations with HUD to update the two agencies' mutual procedures for sharing complaint information. Furthermore, we strengthened our internal procedures for fair housing complaints in several respects. In particular, we established tighter timeframes to facilitate reports to HUD within HUD's statutory time limits for reviewing fair housing complaints. Subsequently, we sent reports to HUD after fair housing complaints were closed and reviewed in Washington.

This procedure was designed so that HUD could review our findings and decide either to accept those findings or pursue the case further. In essence, such a procedure is a form of referral.

We look forward to further consultations with HUD and the other financial regulatory agencies to develop a comprehensive interagency Memorandum of Understanding regarding fair housing complaints.

Q.10 HUD testified last October that the most effective way to detect discrimination is to gather the necessary data and to examine it for patterns of discrimination. What statistical information would prove or strongly suggest discrimination? Do you collect such information? If not, why not?

A.10. HUD's written testimony from the October 1989 hearings before your Subcommittee states, "The most effective way to detect lending discrimination is to gather the necessary data, and to examine the data so as to detect patterns which may reflect discrimination." (Emphasis added). We agree with HUD's written testimony. As a matter of fact, our nondiscrimination examination process is built around the concept of using lending statistics as starting points for further, in-depth analysis of actual loan files. No finding of discrimination can be reached from statistics alone; there must be an accompanying analysis of an institution's lending criteria, underwriting standards, and an applicant's creditworthiness - all factors which are not reflected in any statistics, and which cannot, in any meaningful way, be captured or aggregated for analytical purposes.

We are not aware of any statistics that would either prove or strongly suggest discrimination; as we have mentioned on numerous occasions, statistics do, however, provide examiners with a starting point for conducting discrimination investigations.

Q.11. Will the new statistical information to be gathered pursuant to the recently amended Home Mortgage Disclosure Act (HMDA) be sufficient to strongly suggest discrimination (assuming disparities are present in the data)? Will this data be more useful than existing HMDA data? Will you use it in any way different from existing HMDA data?

A.11. As reflected in our answer to the preceding question, we do not believe that statistics can strongly suggest discrimination. We do believe that disparities in lending data serve a vital role in the examination process by identifying areas for hypothesis testing by examiners. The data must be used in connection with other information gathered through the examination process relating to the demographics of a savings association's community.

The new HMDA reporting system (which substantially mirrors our former LAR/DSR system) should serve to highlight more meaningful disparities in lending patterns due to the capture of applicant income data. We envision that we will be able to use the new HMDA output reports in much the same way that we have used our LAR/DSR reports in the past.

It is important to also mention that OTS-regulated savings associations are required to capture, in their HMDA registers, more information than that required by other reporting entities. First, OTS regulations require savings associations to code the reason for denial in their registers, which will be reflected in the HMDA registers; this field is optional for all other reporting entities. Second, OTS-regulated savings associations are required to record the marital status and age of an applicant, check a box that indicates whether the property that is the subject of a mortgage loan is in the institution's CRA delineated community, and record various data about the loan itself, such as its interest rate and term. These additional data items will be available for the examiner to review during the on-site portion of an examination. Finally, all OTS-regulated savings associations are required to complete loan application registers, regardless of whether they are subject to HMDA.

Q.12. The Center for Community Change has recommended in its testimony that each regulatory agency should adopt regulations similar to the Office of Thrift Supervision's (OTS) nondiscrimination regulation, which prohibits redlining and requires written loan policies to be made publicly available. The OTS believes that requiring all savings associations to make available to potential borrowers their clear, nondiscriminatory loan underwriting standards is an important safeguard to assure uniform application. What do you think of this idea?

A.12. This agency has found these regulations to be effective. Underwriting standards educate the customer about the savings association's expectations, and assure that the association will use consistent standards. The OTS can and does require savings associations to revise vague or imprecise guidelines.

Similarly, savings associations regulated by this agency may not reject a loan, or offer different terms, simply because of the age or location of a property. The agency determined more than ten years ago that the chance of such an approach being discriminatory in effect was so great that it does not have to be shown each time. Rather, the association has to evaluate the individual property, and if rejected, demonstrate with specific details about that property that it does not provide adequate collateral for the loan requested.

Q.13. The National Fair Housing Alliance recommended in its testimony at both hearings that a brochure for mortgage loan applicants explaining how to recognize subtle acts of discrimination and how to file complaints be provided to every loan applicant who is rejected. Most of the regulatory agencies have indicated that the new brochures for consumers would be useful. How much input will the agencies be getting from civil rights specialists in designing these brochures? How will they be different from past brochures? When will they be distributed and how? Will the brochures include phone numbers for the Justice Department's Civil Rights Division, HUD's Fair Housing and Equal Opportunity Division, and local public or private fair housing agencies?

A.13. The Federal Financial Institutions Examination Council has identified a project to produce a brochure or other material that would identify subtle means of discrimination. However, with the press of the CRA Public Evaluation project, the FFIEC has not yet been able to turn its attention to this matter. While the brochure was originally contemplated to be useful to lenders, I will suggest that consideration be given to make the brochures more generic and thus also be useful to consumers. I anticipate that work can begin on this project sometime in the second half of the year, and for this reason I am unable to respond to all of the questions raised. I would encourage input from fair lending organizations, and I anticipate that including the telephone numbers of federal enforcement agencies such as HUD and the Department of Justice would not pose major problems. The same would not be true of the inclusion of local telephone numbers of fair housing agencies, since that would add significantly to the size of the brochure and may likely quickly outdate the brochure because of frequent changes to that type of information.

It should be noted that adverse action notices already advise rejected applicants of their rights, as well as inform them how and where to file a complaint. Therefore, we do not believe there is justification for requiring an additional brochure to accompany the language already embodied in the adverse action notice. A more productive approach might be the one utilized for the "Consumer Handbook on Adjustable Rate Mortgages" and the three consumer's guides on mortgage closings, lock-ins, and refinancings, all of which we published jointly with the Federal Reserve Board. These were widely reviewed and widely distributed on a voluntary basis by trade and consumer groups.

Q.14. You testified during the hearing,"...we are finding some instances where applicants may not have been given the full opportunity to provide a written application..., where there are some underwriting standards that may have the impact of discouraging applications from protected classes...." Please explain these findings in more detail. Also provide specific data on the incidence of these findings and remedial actions taken for each such finding.

A.14. My remarks at the hearing were based upon a limited review of some of the special examinations that we made as a result of identifying institutions with particularly high black-to-white mortgage loan rejection rates. We have had the opportunity to review some of these reports in more detail and to ascertain from our District offices what the supervisory response has been to the reports. Some of these special examinations uncovered various policies, practices, or standards that may have the effect of generally discouraging applications. In and of themselves, several of the items mentioned below are not discriminatory *per se*; they could, under certain circumstances, have a disproportionate impact on credit availability for protected classes.

These policies and/or practices included:

Appraisals

- discounting appraisals for factors already used to determine the fair market value of property. For example, the appraiser would deduct for unreasonable environmental influences such as noise, traffic, etc., when such items are already reflected in the determination of fair market value of property.

Prescreening

- evidence of prescreening identified through discussions with mortgage loan processors. If a prospective applicant's elements of creditworthiness are outside the association's standards, the prospective applicant is informed of likely denial of loan, thus discouraging a formal application.

Practices that May Have Effect of Discouraging Applications

- unrealistically high minimum mortgage loan amounts. This type of policy could have the effect of discouraging applications from persons seeking to finance less expensive housing.

- flat loan fee structure regardless of size of loan. This policy could have the effect of discouraging applications for smaller loan amounts.

- use of substantially more conservative debt-to-income ratios than other lenders in the area.

- use of an underwriting standard that precluded single family dwelling lending in areas devoted to commercial or industrial use, when many low-income neighborhoods were located near factories.

At the conclusion of these examinations, the reports were transmitted to savings association management along with supervisory letters requesting detailed responses regarding measures that management intended to take to address any concerns. This general process is consistent with existing, routine OTS policy. In all but one case to date, our District offices have received responses indicating that the policies or practices have been either corrected or eliminated. In the one exception noted above, the association has been given until the end of July 1990 to respond.

In addition, the OTS District offices conducted board of director meetings addressing the nondiscrimination items in several of the cases.

Q.15. The OTS is the only agency which has issued anti-discrimination regulations. Has OTS ever used these regulations in an enforcement action? Provide several examples.

A.15. As we have testified, our Districts indicate that violations are typically resolved through interaction with senior management without the need for formal enforcement action. Savings associations are directed to remove the violative practices or policies immediately. Supervisory corrective action frequently involves the revision of underwriting guidelines by the institution, resulting in changes to policies and procedures, or the elimination of violative practices. Management often establishes committees or other such control points to review documentation of monitoring information and in some instances, implements computer tracking systems for lending data.

We are aware of one example of a formal enforcement measure that was invoked during the past year. A savings association in the Boston District was found to have committed substantive violations involving the incorrect compilation of LAR/DSR information. The violations resulted from a failure to collect monitoring information. That problem was addressed through a provision in a Cease and Desist Order against the association.

Q.16. Are the OTS's fair lending examination techniques the same as those of the Federal Reserve. The Federal Reserve claims to send out consumer examiners with laptop computers to do analyses of comparable accepted and rejected loan applications.

A.16. Our nondiscrimination and fair lending examination techniques are substantially similar to those used by the Federal Reserve System. The major difference lies in the method used to identify hypotheses for testing during the examination process. Our examiners have had the advantage of having not only a savings association's loan application register to review, but the accompanying output reports, as well. These reports have been required by OTS regulations (12 C.F.R. 528) for the past decade. This enables the examiner to identify hypotheses for testing without the need to first record individual applicant data and sort it. The Federal Reserve process, as we understand it, basically requires the examiner to create the equivalent of a "loan application register" before hypotheses can be identified.

Once the hypotheses are identified, the analytical technique of comparing rejected and accepted loan applicants as used by the OTS, is, to our knowledge, the same as that used by the Federal Reserve System.

The only other significant difference between our procedures and those of the Federal Reserve involves our addition of procedures to evaluate compliance with our own agency regulations relating to nondiscrimination (see A.6.).

Mr. Chairman, you expressed concern at the Subcommittee's May hearings about the mortgage loan acceptance and rejection data that I included in my testimony. I would like to take this opportunity to share more recent information with you.

We have recently completed our computer tabulation of LAR/DSR data from the second half of 1989. That data shows that the black mortgage loan rejection rate decreased to 26.8 percent (roughly a 9 percent decrease as compared to the first half of 1989). The white rejection rate was 13.9 percent (roughly a 7 percent increase as compared to the first half of 1989). Incidentally, the white rejection rate for the second half of 1989 is the highest it has ever been in the 10 years the OTS has been keeping these statistics. The gap, however, between white and black rejection statistics remains at nearly 2 to 1.

We would not characterize the black mortgage loan rejection rate decrease as some sort of victory. We remain concerned about the disparity and its underlying causes. On the other hand, we do not believe that this disparity should be characterized as the result of widespread discriminatory practices by savings associations. Other factors have an impact on the lending disparity. Rising interest rates certainly disqualify more low and moderate income people from obtaining home loans. Furthermore, economic and societal problems facing Black Americans such as high unemployment rates and income inequality, as well as gaps in net worth and rates of business ownership all have an impact.

As a regulator, we are cognizant that the public trust has been placed in our hands. It is our responsibility to enforce the fair lending laws among savings associations through a vigorous examination regimen and to subject violators to the full extent of our enforcement powers. The foundation for this undertaking is now complete and we are striving for full implementation of our program by the end of this year.

Sincerely,

Jerauld C. Kluckman
Director
Compliance Programs

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM
MICHELLE WHITE

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Alan J. Dixon
Chair, Subcommittee on Consumer and Regulatory Affairs
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, D. C. 20510-6075

Dear Senator Dixon:

Thank you for the opportunity to testify May 16, 1990. Enclosed are my answers to the questions you posed.

Question # 1.

You testified "One of the regulators referred to the fact that something didn't smell bad enough to be investigated further. I think that's the seat of the pants approach that most of the regulators take to this. And what I found in the course of my investigations or my consideration of files while at the Office of the Comptroller of the Currency ... (was that) those things that smelled badly to me never even occurred to examiners as being offensive. So I don't think that we can rely upon the examination staff to do the kind of job that's necessary to eradicate discrimination in lending in the United States." Please provide examples of the types of situations which "smelled badly" to you, but were not acted upon by the examination staff.

Answer to Question # 1.

Example # 1

The first instance that comes to mind occurred during my last few months at the Comptroller's. A large Washington based national bank had entered into an agreement to sell mortgages it had originated to another facility. The secondary market buyer made a condition precedent to the purchase of any mortgages that they be secured only by properties be located in Northwest, D.C., which is the overwhelmingly white sector of the Nation's Capitol. The examination team forwarded a copy of the agreement to the OCC Central compliance office for review and recommendations. The existence of the agreement and its discriminatory effect was not criticized in the bank's CRA report of examination.

Example # 2

In the early 1980's, OCC routinely used a data collection system on one-to-four family mortgage loans which required collection of a significant amount of information on each loan by certain national banks. All national banks which received more than 50 home loans the previous year were required to collect relevant documentation. Included in the information collected by such banks and forwarded to OCC was the following: loan amount requested; interest rate requested; number of months to maturity requested; location of dwelling; number of units (1-4); year dwelling built; purpose of loan; name and present address of applicant; age of applicant; marital status; years employed; gross income; proposed house note payment; purchase price; applicant's present liabilities; applicant's net worth; date of application; sex of applicant; race of applicant; appraised value; census tract number; disposition of loan (whether withdrawn before or after terms were offered, denied or terms offered and accepted by applicant.); loan amount offered and accepted; insurance; commitment date; and other information.

Once the above data was collected by the banks, the data was forwarded to OCC-Washington staff, who, in turn, conducted a computer analysis of the bank's lending patterns. Based on all the indicia set forth above, norms for each bank's performance were established. Against these norms, samples of applications submitted by minorities, women, single persons and young and older persons were compared to control group applications. Where the bank's actions were at variance with its norms and the effect could be discriminatory on a protected basis, the loans were highlighted for further investigation by examiners. Although scores of cases were referred for further investigation, never did the commercial, i.e. more experienced, examiners conclude that discrimination had occurred. In those instances where the consumer, i.e. less experienced, examiners, questioned the bank's practices, they were overruled by their superiors.

Washington staff, with backgrounds in civil rights, were not permitted to accompany field examiners into the banks. Our role was limited to reviewing any findings made after the examination was concluded. In addition, the examination staff did not go outside of the bank to inquire of either the applicants whose files were being reviewed or of others who may have had relevant information concerning banking practices. Their investigation was limited to the records of the bank and statements of the employees. (It should be noted that OCC's approach to precluding the civil rights specialists from participating in examinations and limiting the staff to in-the-bank inquiries was very different from that taken by the other agencies which viewed the civil rights staff as part of the enforcement staff.)

These computer identified case investigations were further colored by the fact that the examiners were predisposed to find discrimination only when it appeared to be systemic. One incident of discrimination was not considered significant enough to report or investigate further. Many of these examiners had a background in statistics and economics. They looked for, and reported, only those patterns of discrimination which they considered "significant". One incident, no matter how egregious in its effect upon the individual consumer, did not carry much weight, unless a pattern or practice was unveiled. This approach was a carryover from commercial examinations. Debriefing of examiners revealed that they would not pursue one incident to its natural conclusion, if a pattern of discriminatory practices could not be discerned. The line examiners shared that although they were aware that the examination procedures required full investigations of individual incidents of suspected discrimination, these procedures were not always followed. The examiners simply would not fully investigate individual incidents. There was no way to ensure that full field investigations were being conducted, for the Washington staff did not have line authority over the consumer examiners. The field commercial examiners, who were committed to the concept of conducting full investigations only in those instances where there was shown to be a pattern of discrimination, had such authority.

Debriefing of many examiners revealed that they hated the job of examining for consumer law violations, especially discrimination. They viewed the detection and citing of discrimination as akin to labeling a banker a "moral throwback." Many of the examination staff were young, white and male, who had never personally experienced discrimination of any kind. Most stated that they knew very few minorities, and most were too young to have appreciated the impact of civil rights struggles of the 1960's. Most were firmly convinced that the civil rights legislation had outlived its usefulness. While some consumer examiners conceded that discriminatory practices might exist in poorly managed facilities, most expressed skepticism that discrimination would exist in facilities that were well run.

Another attitude which was of significance was the fact that the examiners saw their mission as preservation of the banking institution which was being examined, as long as it operated in a safe and sound manner. An examiner who found discrimination and exposed it to the consumer affected, invited a claim against the institution, which, in turn, detrimentally effected the bank's net worth. The examiners felt as though they being asked to label bank staff with whom they worked closely as "discriminators". They often opted to avoid such labeling in favor of finding some procedural violation and recommend some corrective measures they deemed appropriate to prevent future violations. These recommendations were more often than not made without consulting with persons who were trained in civil rights enforcement.

Example #3

The examiner staff equated Community Reinvestment Act with Fair Housing/Equal Credit Opportunity Act enforcement. They gave no special emphasis to the fact that the Fair Housing and Equal Credit Opportunity Acts were grounded in constitutional protections. Violation of discrimination laws was considered but one factor in the CRA examination, having little more importance than a failure to post a CRA notice or a failure to provide a map of the facility's service area.

Example #4

Many of the examiner staff refused to see any correlation between appraisal values and race. The staff was unwilling to admit the possibility that an appraisal would be affected by the race of the residents of the area. The fact that comparable housing in black and white sections of a city would be substantially different in price was seen as a matter beyond their ability to affect, or to even raise as a concern in an examination report.

Example #5

OCC approved the use of credit scoring systems by banks which issued credit cards. The characteristics which the scorers take into account include: zip code, income, source of income, family size, length and type employment, and length of residence. To the extent that the zip codes and factors correlated with zip codes are weighted heavily in this calculation, the effect may well result in redlining certain racially identifiable communities. The impact of the use of such systems was discussed and fully considered by the senior Comptroller staff. Despite these discussions, OCC refused to do anything to determine the racial effect on individual applicants or the impact on racially identifiable areas of communities, or to require institutions to make any such determinations. OCC has continued, instead, to authorize the use of such credit scoring systems.

Question # 2

What are your specific recommendations for what the regulatory agencies should be doing differently to enforce the Equal Credit Opportunity Act and the Fair Housing Act? For example, should examination procedures, bureaucratic structure, examination training, and/or complaint response procedures be changed?

Answer to Question # 2

The problem is that the financial regulatory agencies have no real commitment to the enforcement of these Acts. Because the actions of these agencies are cloaked with confidentiality, they are virtually unaccountable. Until an effective method of accountability is established the financial regulators will continue to act as "management consultants" to the industry, and refused to act as an effective enforcement agency to which consumers may turn for assistance. To this end, I would recommend that an auditor general unit be created within each agency. This unit should have access to all confidential information available to examiners, and report directly to Congress on consumer law, most especially the civil rights enforcement efforts of the agencies. Short of establishing this type of unit I do not see any substantive changes being made voluntarily in the enforcement programs at any of these agencies.

The agencies have trained and retrained staff, organized and reorganized their examination personnel. The consumer compliance have been made separate units and, at other times, integrated in with the more experienced commercial staff. The agencies have, on occasion, hidden the civil rights staff away and, at other times, given them relative prominence, such as with the appointment of the OCC Special Assistant for Civil Rights with direct access to the Comptroller. Notwithstanding the mechanics of the individual agency programs, the results are the essentially the same. There are no reported cases of discrimination. Cases are not be forwarded for litigative or administrative enforcement. Consumers who have suffered individual discrimination, and communities which have been redlined, are not being protected.

I am convinced that the goal of equalizing lending opportunities is thoroughly compatible with the safe and sound operation of financial institutes, for nondiscriminatory lending is sound business. I am equally convinced, however, that the industry and its regulators still view lending in certain racially identifiable neighborhoods, and to certain applicant groups, as inherently risky. Until the regulators change their view of the risk, they will have to be monitored closely to ensure they meet their responsibilities to consumers. At this point, I recommend close monitoring. If the situation does not improve, I would recommend that the agencies be relieved of their Fair Housing Act and Equal Credit Opportunity Act responsibilities.

In order to determine whether there is differential treatment on a prohibited basis, data must be collected. The data necessary is similar to that which is collected on home loans, as detailed above. Although each financial regulatory agency has had the authority for at least a decade to require the collection of racial data for other types of loans under 12 CFR 202.13(d), none have required the collection of such data on even a pilot basis. None have anything to determine the nature and extent of racial discrimination in commercial lending, which is closely linked to community revitalization.

The Western Center is presently conducting a study of commercial and other lending patterns of institutions doing business in the City of Los Angeles. Although the study will not be completed until December, 1990, it is apparent that small business owners in racially identifiable sectors of the City have learned to function without bank financing, that they feel as though their areas have been redlined and that they have to go outside their communities to conduct banking business. The extent any or all these impressions and conditions are related to the race of the applicant or the that the residents of the area in which these businesses are located is important to determine. This determination cannot be made without the collection of applicant and area characteristics and conducting a comparative analyses. I would recommend that the agencies promulgate 202.13(d) regulations with respect to other than 1-4 family dwellings.

Once the documentation is collected, the agencies should do a regression analysis to determine what the lending norms are by institution, and whether there are variances from those norms on a protected basis. Variances should then be investigated and enforcement actions taken, if appropriate.

Question # 3.

What changes should be accomplished legislatively?

Answer to Question # 3.

The following are my legislative recommendations:

1. Pass legislation which protects individuals engaged in lending discrimination testing from liability for acts designed to promote the goals of the Fair Housing and Equal Credit Opportunity Acts. Passing legislation of this type will permit testers to determine the nature and extent of discrimination in lending without risking prosecution or civil liability.

2. Fund fair housing and other non-profit groups to conduct testing of credit extensions related to housing, economic development and consumer lending patterns, as well as bank services.

3. Conduct oversight hearings into the practices of the financial regulatory agencies to determine:

> A. How the agencies fulfill their ECOA obligations with respect commercial and non-housing loans, in light of the fact that when they do not collect and analyze the

racial and other information on these loans?

B. Why none of the agencies have promulgated regulations or adopted other enforcement procedures designed to collect information necessary to determine the nature and extent of disparate treatment in non-housing loans pursuant to 12 CFR 202.13(d)?

C. The effectiveness of the financial regulatory programs. For example, OCC and FDIC have computer programs available to them which can identify:

1. the lending norm for each institution;

2. each housing loan which was denied, when it appears it should have been accepted;

3. each housing loan which was accepted, when it appears it should have been denied; and

4. each housing loan which was withdrawn before terms were offered, when it appeared that the loan should have been accepted.

Both agencies have promulgated regulations which require the collection and collation of data on the race, sex, marital status and other relevant information on each applicant, as well as the census tract of each loan.

Each agency should be required to conduct computer runs on a more frequent basis than when examinations are scheduled, which may vary between two and three years, depending on the size of the institution. If variations from the bank's norm which are identiable on the basis of race, sex or any of the other protected categories, then the agencies should be required to determine the basis for the difference in treatment and report on the handling of all such cases to Congress.

D. Whether OCC and FDIC have shared their computer programs designed to analyze the lending norms and practices at variance with those norms for banks under their supervision with other financial regulatory agencies? If they have not, each agency should be encouraged to do so, and the other financial regulatory agencies should be encouraged to develop the data collection systems necessary to effectively compare the treatment individual applicants receive.

E. The effectiveness of the methods used by the agencies to discern the credit market and the market share of the financial institutions which operate in that market. For example, virtually all large cities have assessor/transfer of real estate title information available on computer tape for analysis. In California, all 58 counties' title transfer information is mounted on computer tape. This taped information includes transfers of real estate financed by both the regulated and unregulated institutions. A review of the single family residential lending patterns in one area of Los Angeles whose residents are primarily African-American revealed that federally regulated institutions accounted for only 3% of the market. See attached study by David Rapinsky of the lending patterns in South Central Los Angeles. If a regulatory agency relied only on Home Mortgage Disclosure Act information to determine the effectiveness of a lending institution's program, it would get a very skewed picture, for many unregulated lenders, such as finance companies, and persons financing on the basis of a land contract, are not included in the count.

4. Pass legislation which creates a fair lending auditor general unit within each financial regulatory agency which has access to all confidential information available to the examination staff. This auditor unit should be responsible for assessing the agency's fair lending enforcement program of the agency, and should be answerable directly to Congress.

5. Because securing appropriate housing opportunities often is tied to ensuring job creation and other economic development opportunities in the community, pass legislation which has similar public reporting requirements for non-residential loans as is collected and analyzed on home loans.

6. Amend the Fair Housing and The Equal Credit Opportunity Acts to require the financial regulatory agencies to assess affirmatively the effect of the lending policies and practices of their regulated institutions on the civil rights

of individuals.

7. Commission an independent study of the monetary and social effects of the failure of regulated institutions to lend in racially identifiable areas. One use of such a study would be to assist the legislature in determining whether the ECOA punitive damage limit is appropriate. Another use would be assist courts in determining compensatory damages for community and fair housing groups suing to eliminate redlining.

8. Amend the Community Reinvestment Act to encourage regulated institutions to meet not only the needs of low and moderate income communities, but also those which are racially identiable and underserved.

9. Pass legislation which requires the secondary market lenders to refrain from adopting guidelines, practices or policies which have the purpose or effect of discriminating on a prohibited basis. Pass legislation which requires each such lender to assess affirmatively whether any of its guidelines, policies or practices would have the effect of creating such a result, and report to Congress.

10. Pass legislation which requires those agencies which allocate tax credits for the development or bonding of affordable housing to assess the impact its allocations have had on the equal housing and employment opportunities for its residents.

If you have any questions, please contact me.

Very truly yours,

Michelle White

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RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM ROBERT J. HERRMANN

Comptroller of the Currency
Administrator of National Banks

Washington, D.C. 20219

August 9, 1990

The Honorable Alan J. Dixon
Chairman
Subcommittee on Consumer and Regulatory Affairs
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, D.C. 20510-6075

Dear Mr. Chairman:

This is in response to your request that we submit answers to follow-up questions from the May 16, 1990 oversight hearing on discrimination in home mortgage lending.

Enclosed are the OCC's responses. I appreciate the opportunity that you have provided us to further explain the agency's position on the issues you have raised. If I can be of further assistance, please do not hesitate to call me.

Sincerely,

Susan F. Krause

Susan F. Krause
Senior Deputy Comptroller
for Bank Supervision Policy

Enclosure

Q.1 **In how many instances over the past three years has your agency found substantive violations involving mortgage race discrimination of the Fair Housing Act or the Equal Credit Opportunity Act (ECOA) while conducting examinations? Explain how each of these substantive violations was resolved.**

Answer From January 1, 1987 through April 30, 1990, our examiners cited 140 violations of the substantive provisions of the ECOA. (See Comptroller's Handbook for Consumer Examinations, Sec. 501.002.1). No violations of the Fair Housing Act were cited during this time period. However, most violations of the Fair Housing Act involving illegal discrimination in lending are also violations of the ECOA. Seventeen of the 140 ECOA violations occurred in real estate loan departments. We obtained this data from our automated information system which is designed to retrieve information by regulation citation.

When violations of any law, including ECOA, are discovered, we require the bank to immediately discontinue the illegal practice. We also require the bank to review its systems to identify the cause of the problem and to implement corrective action to prevent future violations. Most banks comply voluntarily.

If violations of certain substantive provisions of the Fair Housing Act and the ECOA are discovered, the bank is required to take corrective action in accordance with the interagency policy statement, Enforcement of the Equal Credit Opportunity and Fair Housing Act. The policy statement requires efforts to correct the conditions that were the result of the violation. A copy of this policy statement is attached.

A violation involving possible racial discrimination has been referred to the Department of Justice for resolution.

Q.2 **How many fair lending written complaints involving mortgage race discrimination did your agency receive over the past three years? How many of these complaints led to a finding of a substantive violation? Explain how each of these violations was resolved.**

Answer In the three year period ending March 31, 1990, the OCC recorded 34 complaints alleging racial discrimination in real estate lending. Our investigation of these complaints, which includes direct contact with the banks involved, revealed no violations of fair lending laws. One case was found to be the subject of private litigation. The OCC does not intervene when complaints are in litigation or have been litigated previously.

Q.3 **The Toledo Fair Housing Center received 102 mortgage discrimination complaints over the past three years just from the Toledo area - of which about 40% showed probable cause. How many mortgage discrimination complaints did you receive for the entire U.S.? Is the number roughly proportional to the Toledo experience? If it is significantly lower, what factors might account for the difference?**

Answer As we noted in our answer to the previous question, in the three years ended March 31, 1990, the OCC received 34 written complaints alleging racial discrimination in real estate lending. This number clearly is not proportional to the 102 complaints received from the Toledo area by the Toledo Fair Housing Center (Center).

It is not surprising that the Center received proportionally more complaints than the OCC and the other Federal financial institution regulators. The Center used funds received from a private foundation, matched with Community Development Block Grant funds, to run a series of television programs and advertising campaigns in the minority press. According to the Center's testimony, a typical solicitation would read, in part, "If you are turned down for a home loan for any reason or if the lender changes the terms or conditions of your loan contact the FAIR HOUSING CENTER." Additionally, the Center apparently received complaints about all types of home mortgage lenders. The testimony does not provide any information on the number of complaints about the actions of commercial banks. While national banks are significant home mortgage lenders, they are a relatively small part of the total market. Also unclear to us are the evaluation criteria used by the Center in their determination of the difference between "possible" discrimination and "probable" cause.

Q.4 **How many hours out of an examination will an examiner spend on fair lending enforcement? How many on Community Reinvestment Act (CRA)? How often are these exams done?**

Answer Because the size of national banks varies greatly, the average number of hours spent on fair lending examinations may not be a useful measure of the OCC resources devoted to examinations for compliance with fair lending laws. In 1989, the OCC devoted 22 thousand work hours directly to compliance with fair lending laws. The average time by size of national bank is as follows:

FAIR LENDING

Asset Size	Average hours
over $10 billion	86
$1 billion - $10 billion	65
$300 million - $1 billion	50
$100 million - $300 million	27
$50 million - $100 million	25
under $50 million	20

An additional 22 thousand work hours were devoted to assessing the quality of management, audits, controls and systems. This effort is extremely important to our supervisory process but can not be readily allocated to individual phases of the examination process. Additionally, these times do not include offsite supervisory activities such as review and processing reports of supervisory activity and monitoring of corrective action.

We have estimated that 20 percent of a consumer compliance examination is devoted to CRA.

A total of 189,000 onsite work hours were devoted to compliance with consumer protection and fair lending laws in 1989. Based on this estimate, the OCC devoted about 38,000 work hours to CRA examinations in 1989 as follows:

COMMUNITY REINVESTMENT

Asset Size	Average Hours
over $10 billion	135
$1 billion - $10 billion	80
$300 million - $1 billion	44
$100 million - $300 million	28
$50 million - $100 million	24
under 50 million	18

Fair lending compliance is enforced as part of the OCC's Compliance Program. One aspect of the Compliance Program is a thorough examination of all banking companies with total assets in excess of $1 billion every two years. In addition, a random sample of banks under this threshold is examined annually.

Q.5 **In your exams, do you check whether certain minority neighborhoods have higher rejection rates than comparable white neighborhoods?**

Answer No, examiners use Home Mortgage Disclosure Act (HMDA) data to determine where home loans are made and to identify neighborhoods where there is little apparent lending. The data provided under the recently revised HMDA will not be available until late in 1991, so examiners will not be able to readily identify minority neighborhoods with higher rejection rates until then.

Q.6 **What are your examiners trained to do when they find a lending institution with a policy of requiring a minimum loan size, lot size, or income level? A maximum age of the house? That the neighborhood was stable or improving? How many institutions have been cited for this?**

Answer Our examiners are taught that these types of policy statements should be considered under the "effects test," a judicial doctrine developed in cases involving employment discrimination, but with little guidance on how the courts might apply the effects test to the area of credit discrimination. If examiners identify credit underwriting standards that appear neutral on their face but may have a discriminatory effect, they are taught to bring this to the attention of management. The compliance examinations procedures instruct the examiner to discuss policies or procedures that may have the effect of discrimination in the report of supervisory activity. We are aware that such comments were included in 13 reports from April 1987 through year end 1989.

Q.7 **If a loan were denied because of a low appraisal on the property - as is often the case in minority neighborhoods - will the examiner check this in its computerized sampling technique? Will the examiner be able to check whether the appraisal itself was based on illegal discrimination?**

Answer No, examiners are instructed to verify that the bank uses the nondiscriminatory standards of the American Institute of Real Estate Appraisers and the Fair Housing Act. Examiners can identify obvious discriminatory practices such as racial notations on appraisal reports. However, they are not trained as appraisers and have limited ability to identify discriminatory appraisal practices. The OCC has finalized its standards for real estate appraisals. The regulation implements Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989. The rule provides added assurance that appraisals are performed in accordance with uniform standards by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision. We recognize the fact that the final rule contains a cut-off for which appraisals do not have to be prepared by certified appraisers. Therefore, we will revisit our examination procedures in light of the regulation to ensure that the banks' standards continue to be nondiscriminatory.

Q.8 **Some regulatory agencies have testified that their examination techniques test for discriminating practices by comparing rates of one financial institution with others in the same area. Do wide disparities exist between institutions? Give some examples (without revealing names). Various aggregate studies imply that lenders across the board may be discriminating. Would not this technique then suggest that no problem exists when in fact there is a major problem?**

Aggregate information on lending or rejection rates has limited use for identifying illegal discrimination. The treatment of applicants by individual lenders must be compared to identify illegal discrimination. Comparing the lending volume of one lender with the aggregate of other lenders in an area may be useful for evaluating that lender's record of helping to meet the credit needs of its community. It might also be a useful technique for targeting examination efforts. However, ultimately, the actions of any lender must be compared against its credit standards and its ability to meet community credit needs.

Q.9 **No agency has referred cases of possible discrimination to the Department of Justice for prosecution. Have you referred any cases to the Department of Housing and Urban Development?**

Answer In May of this year, the OCC referred to the Department of Justice a case of apparent racial discrimination in the sale of other real estate owned.

While we have not referred cases to the Department of Housing and Urban Development (HUD), consumers are advised by posters displayed in all national banks that they may file a complaint with HUD.

Q.10 **HUD testified last October that the most effective way to detect discrimination is to gather the necessary data and to examine it for patterns of discrimination. What statistical information would prove or strongly suggest discrimination? Do you collect such information? If not, why not?**

Answer Home Mortgage Disclosure Act data can be used to identify areas where there is little or no lending. However, it provides no information on why the patterns of lending occur. To establish the presence of discrimination would require a specific statistical model for each lender. The model would control for the factors used in the lender's credit decisions. To identify possible discrimination, a more general statistical model may be used. The OCC uses such a model. The Fair Housing Home Loan Data System evaluates home loan credit decisions using three financial ratios commonly used in home loan underwriting. It identifies applications in which the credit decision appears to be associated with the race (or other prohibited basis) of the applicant. Because the analytical process does not consider all factors in the credit decision (for example, credit history), the results of the statistical analysis do not necessarily indicate discrimination. The statistical tests direct the examiner's attention to those files where discrimination is most likely to have occurred.

Q.11 **Will the new statistical information to be gathered pursuant to the recently amended Home Mortgage Disclosure Act (HMDA) be sufficient to strongly suggest discrimination (assuming disparities are present in the data)? Will this data be more useful than existing HMDA data? Will you use it in any way different from existing HMDA data?**

Answer The OCC, as a member of the Federal Financial Institutions Examination Council (FFIEC), participated actively in the development of the HMDA disclosure statements for individual reporting institutions and the aggregate reports for each Metropolitan Statistical Area (MSA) in the United States.

These reports were designed to be a primary vehicle through which to carry out Congress' expressed intent to "maximize public disclosure" of lending data, placing the "highest priority on the collection of analytically useful data ... to identify and eliminate discriminatory lending practices."

The use of the expanded reports will be similar to the use of the existing reports. However, the expanded reports will be more useful than the existing HMDA data in assessing a financial institution's geographic distribution of credit extensions, credit applications, and credit denials. If disparities are present in the data, we believe that the new reports will help to detect possible discriminatory practices.

Because of the magnitude of the reports, it will probably take some time and experience with the new data to determine its specific and most effective use. To do a comprehensive, accurate and fair assessment will require the allocation of significant amounts of time and resources. For example, in 1989, Bank of America (B of A) reported loan originations in 23 MSAs; thus, 23 tables were generated for this bank, and each one of its individual MSA tables could be compared with the 6 aggregate tables for the same MSA. Assuming B of A has not increased or decreased the number of MSAs under which it will report 1990 activities, during 1991, the FFIEC will be generating 759 tables of approximately 989 pages in length for this bank alone. To assess the entire bank's performance relative to other reporting institutions, these 759 individual tables will need to be compared to the 805 aggregate tables of approximately 1,495 pages that will cover the same MSAs.

Further, evaluating a financial institution's geographic distribution of credit extensions, credit applications and denials based on the HMDA data is not sufficient to conclude that it is discriminating. The examiner must compare the bank's treatment of individual applicants, giving consideration to factors such as the applicants' credit history to establish the presence of discrimination.

Q.12 **The Center for Community Change has recommended in its testimony that each regulatory agency should adopt regulations similar to the Office of Thrift Supervision's (OTS) nondiscrimination regulation, which prohibits redlining and requires written loan policies to be made publicly available. The OTS believes that requiring all savings associations to make available to potential borrowers their clear, nondiscriminatory loan underwriting standards is an important safeguard to assure uniform application. What do you think of this idea?**

Answer All of the illegal practices contained in the OTS regulation are already illegal under the FHA (and its implementing regulations) and, except for condition of handicap and familial status, the ECOA (and its implementing regulation). Moreover, the OCC has encouraged the Boards of Directors of all national banks to adopt written loan policies for decades. The vast majority have done so. Rarely are national bank loan policies found to contain illegal discriminatory provisions. Verification of consistent application of an articulated loan policy is a relatively easy task for an examiner. It would be virtually impossible for a consumer.

Q.13 **The National Fair Housing Alliance recommended in its testimony at both hearings that a brochure for mortgage loan applicants explaining how to recognize subtle acts of discrimination and how to file complaints be provided to every loan applicant who is rejected. Most of the regulatory agencies have indicated that new brochures for consumers would be useful. How much input will the agencies be getting from civil rights specialists in designing these brochures? How will they be different from past brochures? When will they be distributed and how? Will the brochures include phone numbers for the Justice Department's Civil Rights Division, HUD's Fair Housing and Equal Opportunity Division, and local public or private fair housing agencies?**

Answer The OCC will be working with the other members of the FFIEC to develop a fair lending brochure during the second half of this year. We hope to have the brochure available for distribution early in 1991. No decisions have been made on how or when the brochure will be made available.

We expect to seek the assistance of civil rights specialists and organizations as well as representatives of lenders and other government agencies on the form and content of the brochure. We expect to include the address of the Civil Rights Division of the Department of Justice and the Assistant Secretary for Fair Housing and Equal Opportunity, Department of Housing and Urban Development. At their request, we would also include their telephone numbers. Because of the technical difficulties in doing so, we do not expect to include the names and addresses of local fair housing agencies. We will consider including space for insertion of information on local agencies.

The available brochures we have seen contain descriptions of the requirements of the ECOA and FHA. We believe the new brochure should help people relate the requirements of the law to prohibited practices.

Q.14 **How often does the Office of the Comptroller of the Currency (OCC) actually do on-site fair lending examinations of banks that it supervises, which have less than $1 billion in assets?**

Answer Approximately 2,300 compliance examinations of community banks were conducted in the two years ended December 31, 1989. The OCC does not schedule its compliance examinations of banks under $1 billion in assets based on the passage of time. As part of its program to promote compliance with law, including fair lending laws, the OCC annually examines a random sample representing 16% of these banks. The random chance of being selected for a thorough compliance examination is a strong incentive for compliance. In addition to the random sample, many other banks are selected for examination each year because of concerns of the supervisory examiners.

Q.15 **Your testimony states that banks with over $1 billion in assets are examined every two years, but only a random sample of banks with fewer assets are examined. Your testimony then explains that you conduct targeted exams of banks not included in the sample - roughly 600 to 700 such exams a year. How many of these targeted exams have you done because you suspected inadequate compliance with consumer protection laws in general? How many because of CRA? How many because of fair lending potential problems?**

Answer Our supervisory information system does not permit retrieval of aggregate information on what conditions or events triggered the targeted examinations of banks not selected for the compliance program sample. Under our supervisory process, an examiner is responsible for the complete supervision of a small portfolio of banks. The examiner develops a supervisory strategy for each bank based on personal knowledge of the bank's operations. While we are aware that some banks were targeted for examination because of concerns about fair lending and CRA, we believe most examinations were triggered by more general concerns for promoting compliance with law.

Q.16 **The OCC is the agency with the least interest in having a separate Consumer Compliance Division. Both the Federal Reserve and OTS insist that separate training and career paths are critical to strong enforcement. Don't they have a good point?**

Answer There is no evidence that state chartered banks or thrifts have better records of compliance with law than national banks. Effective enforcement requires examiners who have a broad understanding of banking operations and practices and the bank supervision process. We believe that National Bank Examiners should have broad experience in the bank supervision process before they start to develop specialized expertise in any area, including compliance with community, consumer protection and fair lending laws. To conduct effective assessments of bank compliance with these laws, the examiner must first understand all facets of banking and how they interact with one another.

The requirement for a broad background does not negate the need for experts who, once commissioned as National Bank Examiners, are used in banks targeted for compliance examinations. The OCC has compliance experts who perform examinations in the largest banks and also provide consultative assistance to our examining staff on complex, sensitive, and unusual consumer compliance issues.

Moreover, the examination process is only one component of an overall supervisory strategy to promote compliance with law. The OCC's use of thoroughly trained examiners who have expertise in specific disciplines is only one aspect of an effective and efficient program to enhance compliance with law, including fair lending laws. Other aspects of the program include: developing monitoring tools and procedures for off-site supervision of banks; educating examiner, bankers and community groups; strictly correcting noncompliance, and acting to simplify regulations.

Q.17 **The testimony of the Center for Community Change from the October 24, 1989 hearing states that data obtained from the OCC by Freedom of Information Act requests, showed that minority applicants with a high probability of approval were actually rejected far more often than white applicants with a high probability of approval. Explain how this can be true and you still find few anti-discrimination violations.**

Answer The information the Center for Community Change obtained was aggregated data from the OCC's Fair Housing Home Loan Data System (FHHLDS) from the early 1980's. The specific cases involved in the information provided to the Center for Community Change were followed up during examinations, and a review of the files did not disclose discriminatory treatment.

The FHHLDS was developed as a tool for examiners. It provides the examiner with a relatively short list of cases in which the applicant appears to have been treated differently from most other applicants.

The system has limitations. The statistical analysis uses three ratios (loan to value, monthly housing expense to monthly income, and total monthly debt expenses to monthly income) to assign each application an estimated probability of acceptance. However, this probability of acceptance is only an initial estimate because the system does not control for the numerous other factors involved in real estate loan credit decisions. These factors include length of employment, credit history, length of residence and other factors that would predict the ability and willingness of applicants to repay debt. Therefore, the examiner uses the FHHLDS to flag potential cases of discrimination but has to consider other factors in each case to confirm discriminatory treatment.

Q. 18 **The testimony from the Western Center on Law and Poverty charges that the OCC did not properly investigate a complaint of discrimination by the Concerned Citizens of South Central. According to the testimony, the OCC's response to the complaint was to state that the issue would be investigated during the bank's next examination but no indication was provided when the exam would occur. Did the response to this complaint follow standard OCC procedures? Do you believe the OCC's response was sufficient?**

Answer We believe the complaint was processed appropriately. Consumer complaints are processed by specialists in each district office who are trained in all consumer protection and fair lending laws. The complaint specialists operate with written guidelines. Our procedures require that we review information submitted by an individual consumer and the bank involved. Once we have reviewed all information relevant to the individual complaint, we determine what follow-up actions are appropriate.

The complaint in question contained broad allegations about the bank's failure to market its credit products in South Central Los Angeles and its failure to lend in the minority areas of the city. It did not contain the names of any individuals who alleged they had been treated illegally. Nevertheless, we contacted senior management of the bank in question and they, in turn, have been in contact with the Concerned Citizens of South Central.

We make every attempt to assist individual consumers who complain about their treatment by national banks. We believe that broad based allegations are most effectively and efficiently investigated through our normal supervisory process and examination procedures.

Q.19 **Your testimony refers to the two assessment factors considered in CRA examinations which relate to discrimination. Would a lender be able to "fail" these factors but still "pass" its CRA exam? Testimony from the Center for Community Change claims, "Unfortunately, the guidelines as currently written do not automatically bar those lenders that are found to be engaged in discriminatory practices from receiving a satisfactory or higher CRA rating." If a discrimination violation is found, have examiners been instructed to include this in the CRA written evaluation which will be publicly disclosed?**

Answer If a national bank has been found to have engaged in discriminatory practices during the assessment of performance, performance under other assessment factors would be negatively affected. Therefore, any financial institution found to be discriminating on a prohibited basis under the antidiscrimination laws and regulations would not be rated satisfactory or higher under the Uniform Interagency Community Reinvestment Act Assessment Rating System. As required by the Financial Institutions Reform, Recovery and Enforcement Act of 1989 amendments to the Community Reinvestment Act of 1977, the CRA written performance evaluation that is made public will state the conclusions. If banks are found in violation of the substantive provisions of the antidiscrimination laws, examiners have been instructed to include that fact in the CRA performance evaluation.

Q.20 **Are the OCC's fair lending techniques the same as those of the Federal Reserve? The Federal Reserve claims to send out consumer examiners with laptop computers to do analysis of comparable accepted and rejected loan applications.**

Answer In general, we believe the OCC's fair lending examination procedures are similar to the Federal Reserve and other depository institution regulators. We are familiar with the Federal Reserve's personal computer application. It is a spreadsheet application that provides counts of the number of applicants by various classes, such as male and female or white and black. The application also provides listings of applications by class in which the decision is inconsistent with the bank's articulated loan policy. It requires entry of the bank's articulated lending standards and numerous items for each loan selected for review.

The OCC has developed a sophisticated statistical analytical system, the Fair Housing Home Loan Data System (FHHLDS). The FHHLDS requires national banks to submit information on a sample of home loan applications in advance of an examination.

The system uses a statistical technique to compare the treatment of individual applicants to a hypothetical loan policy based on the bank's actual practice (as opposed to its articulated loan policy). Applicants who appear to have been treated differently from the norm are identified, and a statistical test is performed to determine if there is a relationship between certain characteristics of the applicant such as race or sex and the apparent differential treatment (either favorable or unfavorable). The system provides the examiner with a list of files where illegal discrimination (if present) is most likely to have occurred. These files are reviewed during an examination to ensure the applicants did not receive discriminatory treatment. The system is limited because the statistical tests require sample sizes greater than the application volume of most community banks. However, in most smaller banks, an examiner can efficiently compare the treatment of a sample of applicants manually. Because most national banks receive relatively few home loan applications, often the examiner can review all applications from minorities for the previous 25 months, which is the record retention period required by the Equal Credit Opportunity Act and the FHHLDS.

Appendix—Policy Statements

Enforcement of the Equal Credit Opportunity and Fair Housing Acts

This document sets forth the general policies that the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency (hereafter referred to as the "agencies") will generally apply in enforcing the Equal Credit Opportunity Act and the Fair Housing Act. Coordination among the agencies is desirable to bring about uniformity in the administrative actions that will be taken when violations of the acts are detected. The Federal Home Loan Bank Board has elected not to participate in this joint policy statement because it believes its existing policies are both sufficient and compatible with the joint statement.

Supplementary Information. The following enforcement policy statement is issued pursuant to the enforcing agencies authority under the Equal Credit Opportunity Act (ECOA) (15 USC 1691, et seq.), the Fair Housing Act (42 USC 3601, et seq.); and under 8(b) of the Federal Deposit Insurance Act (12 USC 1818(b)) for the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation, and under the Federal Credit Union Act (12 USC 1786(e) (1)) for the National Credit Union Administration.

The agencies believe it appropriate to remind institutions of their responsibilities under these laws and that the agencies will vigorously enforce them. Creditors will be required to institute procedures to assure that all violations of the acts, including those not cited in this policy statement, will not recur. In addition, failure to comply with certain specific provisions of the acts has been judged by the agencies to be particularly serious and usually to warrant retrospective action to correct the condition resulting from the violations.

Equal Credit Opportunity and Fair Housing Acts Enforcement Policy Statement. This enforcement policy statement ensures that the rights of credit applicants are protected by requiring creditors to take corrective action for certain, more serious past violations of the Equal Credit Opportunity and Fair Housing Acts as well as to be in compliance in the future. In an effort to achieve that objective, the agencies will encourage voluntary correction and compliance with the acts. Whenever violations addressed by this policy statement are discovered, the creditor will be required to take action to ensure that such violations will not recur and to correct the effects of violations discovered.

The agencies will generally require the creditor to take action to correct conditions resulting from violations occurring within 24 months prior to the discovery of violations by an agency. An exception is violations concerning adverse action notices for which corrective action will be required for violations occurring within six months prior to discovery.

Violations in the following areas are considered serious by the agencies and will usually be subject to retrospective corrective action:

- Discouraging applicants on a prohibited basis in violation of the Fair Housing Act or 202.4 or 202.5(a) of Regulation B.
- Using credit criteria in a discriminatory manner in evaluating applications in violation of the Fair Housing Act or 202.4 through 202.7 of Regulation B.
- Imposing different terms on a prohibited basis in violation of the Fair Housing Act or 202.4 or 202.6(b) of Regulation B.
- Requiring cosigners, guarantors or the like on a prohibited basis in violation of 202.7(d) of Regulation B.
- Failing to furnish separate credit histories as required by 202.10 of Regulation B.
- Failing to provide an adequate notice of adverse action under 202.9 of Regulation B.

This policy statement will not:

- Preclude the use of any administrative authority that any of the agencies possess to enforce these laws.
- Limit the agencies' discretion to take other action to correct conditions resulting from violations of these laws.
- Preclude referral of cases to the Attorney General.
- Foreclose a credit applicant's right to bring civil action under the Equal Credit Opportunity or Fair Housing Acts or to file a complaint with the Department of Justice or the Department of Housing and Urban Development for violations of housing laws.
- Supersede or substitute for any regulations or enforcement policies issued by any of the agencies or the Department of Housing and Urban Development under the Fair Housing Act.

Appendix—Policy Statements
Supplementary Enforcement Policy for the Equal Credit Opportunity and the Fair Housing Acts

Part I

This document supplements and expands upon the Equal Credit Opportunity and Fair Housing Acts (the "acts") Enforcement Policy Statement recommended by the Federal Financial Institutions Examination Council (FFIEC) on September 10, 1981 and adopted by the Comptroller of the Currency.

The policy statement was issued to national banks to remind them of the seriousness of certain violations of the acts and to inform them that such violations will be dealt with by the agency retrospectively as well as prospectively. This document provides guidance by describing various actions for correcting the following substantive violations:

- Discouraging applicants on a prohibited basis.
- Using credit criteria in a discriminatory manner in evaluating applications.
- Imposing different terms on a prohibited basis.
- Requiring cosigners, guarantors and the like, on a prohibited basis.
- Failing to maintain and furnish separate credit histories.
- Failing to provide proper adverse action notification.

The OCC generally will use those actions described in Part II of this document, as appropriate, to correct the conditions caused by the violation. However, if the OCC believes that different corrective action would be more suitable, this policy does not preclude our discretion to use it.

This policy provides guidance for correcting both the conditions and practices resulting from violations of the acts. When violations of the acts addressed by the policy statement are discovered, the institution should be required to adopt a written compliance program to ensure that they will not recur. The program normally should include employee training in the requirements of the acts and the establishment of an internal controls program. The institution may be required to include a written loan policy or written appraisal standards in the compliance program should the violations of the acts so warrant.

Part III of this document contains three examples of how this policy might be implemented.

Part II

1. *Discouraging Applicants on a Prohibited Basis in Violation of the Fair Housing Act, or Section 202.4 or 202.5(a) of Regulation B*

When this violation is discovered, the institution should be directed to adopt, in consultation with the enforcing agency, a program to reverse and overcome the effects of those practices by the institution that have limited participation in its credit programs by the discouraged group.

Each program normally should be tailor-made and designed to increase applications from the discouraged group.

The program should include an in-house training program and such marketing techniques as are necessary to encourage or solicit applications from the discouraged groups. Among the techniques that have proven successful are:

- Advertising in appropriate media, particularly through the depiction of members of the discouraged group as successful applicants.
- Establishing new business relationships with real estate brokers, automobile dealers, or other arrangers of credit who generally service the discouraged group.
- Sending direct mailings to members of disfavored classes.
- Contacting representative community groups to be employed in the credit evaluating process.
- Sponsoring credit education programs.

If specific individuals have been identified who have been discouraged on a prohibited basis from applying for credit, the institution should be required to send to all such discouraged applicants a notice that contains:

- The solicitation of a (new) application.
- A disclosure that the applicant has 60 days in which to (re) apply.

2. *Using Credit Criteria in a Discriminatory Manner in Evaluating Applications in Violation of the Fair Housing Act or Sections 202.4 through 202.7 of Regulation B.*

When this violation is discovered, the institution should be required to identify all applicants affected by the discriminatory standard(s) within the 24-month period prior to discovery of the violation by the enforcing agency.

These applicants will be sent a notice that includes:

- The solicitation of a new application by the institution.
- Disclosure that the applicant has 60 days in which to reapply.
- A description of the conditions under which any refund or reimbursement will be made.

In addition to the above customer notification requirements, the institution should be instructed to notify any party it previously informed of the rejection and inform that party to correct the applicant's credit history by deleting the previously reported rejection.

The institution should be required to offer to refund any fees or costs associated with submitting or processing the original application in the notice. This refund offer should include, at a minimum, application, appraisal, prepaid, and credit check fees. Upon re-application, the institution should not be allowed to require applicants to pay fees or costs associated with submitting or processing the new application. Such fees may be charged, however, if the application is approved. The sum of those fees must be the lesser of the total in effect at the time of original application.

In evaluating borrowers' applications, the institution should be directed to use the creditworthiness standards in effect at the time of the original applications, absent any discriminatory elements, or those currently in effect, whichever are more favorable to an applicant.

If the new applications are approved and are for credit other than open-end, the terms offered will be those currently in effect or those in effect at the time of the original applications, whichever the agency deems most appropriate.

If applicants reapply and new applications are approved, but the applicants have obtained alternative credit in lieu of that denied on a prohibited basis, the agency will consider requiring the creditor to refund fees and costs required by subsequent creditors to pay off the alternative credits. For applicants who have not obtained alternative credit, the agency should require that the costs for submitting and processing new approved applications will be the lesser of the total currently being charged by the institution on the total in effect at the time of the original applications.

The institution should be allowed to terminate the reapplication offer if it does not receive a reapplication within 60 days.

3. *Imposing More Onerous Terms on a Prohibited Basis in Violation of the Fair Housing Act or Section 202.4 or 202.6(b) of Regulation B.*

When this violation is discovered, the institution should be required to identify all such loans and notify consumers within 60 days of the corrective action. The institution should be required to offer to substitute nondiscriminatory terms for any terms illegally required and reimburse applicants for any money illegally required.

When the institution has improperly imposed a higher annual percentage rate, higher finance charges, insurance, or other loan fees, such as points on a real estate loan, the institution should be instructed to reimburse consumers the money illegally required.

When the institution has imposed other more onerous terms, such as requiring higher downpayments, shorter maturities, or stricter collateral requirements, it should be instructed to offer to change the account from the terms illegally required to the terms for which applicants should have qualified. The institution should be instructed that no fees for processing such changes may be assessed, and that the offers must state that fact.

The method for reimbursement to applicants should be the lump sum or the lump sum/payment reduction method, at the institution's option. In the case of a loan which is in default, the institution should be instructed to reduce the balance with any monies illegally required.

4. *Requiring Cosigners on a Prohibited Basis in Violation of Section 202.7(d) of Regulation B.*

When this violation is discovered, the institution should be instructed to identify all affected applicants and release additional parties where appropriate. The institution should be instructed to absorb any cost associated with the illegal requirements, such as recording or filing fees, or fees for consumer reports, imposed on applicants by the institution or by any third party in connection with the illegal requirement.

If an applicant was individually creditworthy, but a cosigner, guarantor, or other additional party was required in violation of the act, the institution should be directed to notify all parties that the additional party will be released unless other instructions are received within 30 days from the parties to the debt. The notice of release should be sent to all contractually liable parties.

If an additional party was necessary to support the extension of credit requested, but the institution restricted the applicant's choice of parties on a prohibited basis, the institution should be directed to include in the notice sent to all parties that the applicant may substitute a creditworthy party to provide the necessary support to maintain the extension of credit. The notice also should state that the additional party originally required will be informed of the effective date of the release, provided a suitable substitute is found. The institution should be instructed that the offer to accept another party should remain in effect for at least 60 days. If an applicant was individually creditworthy, but was rejected because of inability or unwillingness to furnish a cosigner, guarantor, or other additional party required by the institution in violation of the act, the appropriate remedy is provided in No. 2 above.

If an additional party was necessary to support the extension of credit requested, and the applicant offered a financially responsible party but was rejected because of inability or unwillingness to furnish an alternative party or particular additional party specified by the institution in violation of the act, the appropriate remedy also is provided in No. 2 above. If any changes to the account are made regarding the cosigner, guarantor, or other additional parties, the institution should be directed to report them to the appropriate consumer reporting agency.

5. *Failing to Furnish Separate Credit Histories for Married Persons in Violation of Section 202.10 of Regulation B.*

When this violation is discovered, the institution should be instructed to identify all affected applicants and take the following corrective actions as appropriate within 30 days: (1) designate joint accounts to reflect the participation of both spouses and comply with the requirements of section 202.10(a)(2) and (3); (2) notify consumer reporting agencies to which it has furnished credit information of the separate credit histories improperly or inaccurately and request them to amend their records to reflect such histories properly; and (3) notify the account holder that this information was not reported accurately, that it may have been the cause of a credit denial from other creditors, and that if credit was denied on the basis of an insufficient or nonexistent credit history or credit file, the applicant may want to reapply.

If the institution has failed to obtain sufficient information for accounts held by married persons, the institution should be directed to request the necessary information it lacks within 30 days.

Upon receipt of the information, the institution should be instructed to take the reporting and notification actions specified in the preceding paragraph.

6. *Failing to Provide Notices of Adverse Action in Violation of Section 202.9 of Regulation B.*

If the institution has failed to send notices of adverse action to applicants against whom adverse action has been taken, the institution should be directed to identify such applicants and send adequate adverse action notices.

If the institution has failed to provide an adequate notice of adverse action or has failed to provide an accurate statement of the reasons for denial to applicants against whom adverse action has been taken, the institution should be directed to send an adequate adverse action notice to all affected applicants.

The corrective action time period for violations of this section is six months prior to the discovery of the violation.

Part III

The following case studies illustrate the application of the foregoing corrective actions to specific situations.

Case I:

The examination revealed that some, but not all, loans to minority groups were made with more onerous terms than the creditor's average loan for any given time period. These applications were submitted to the loan committee with a stated rate of ¼ point above those for nonminorities. In five cases, the applications involved an extra point, upon the recommendation of the loan officer.

These loans were traced to two of the creditor's 12 loan officers. Both worked in the same branch office. The examiner reported that the creditor received few applications from minorities living in the area served by the branch.

1. To prevent recurrence of the violation, the agency required the creditor to:
   - Sign a written agreement that described the violations and specified the corrective action the creditor would take.
   - Issue a memorandum to employees describing the problem and directing that loan applications should be taken for the same terms, regardless of the identity of the applicant(s).
   - Revise the written underwriting standards to incorporate the instructions issued in the memorandum above.
   - The agency further required the creditor to conduct training for all loan officers to assure that they are familiar with the acts and with the creditor's nondiscriminatory underwriting policies.
2. Because this practice, limited to one branch, may have presented a discriminatory impression to the area served by the branch, the agency also required the creditor to take the following actions to correct this preception.
   - Place advertisements, including the current terms at which credit is available, in local newspapers, especially any having circulation in the community served by the branch, that solicit applications for credit.
   - Inform real estate brokers who regularly deal with the adversely affected groups of the lender's credit and underwriting standards.
   - Conduct a credit education course in the community to include information on how to qualify for credit and how to prepare a credit application.
3. To correct conditions caused by the violation, the agency required the creditor to:

- Identify the individuals affected by this policy and advise them that their rates were adjusted.
- Correct the loan contracts to eliminate the higher interest rate, with no charge to the borrowers for this action.
- Reimburse the five individuals for the extra point they had been charged and refund the overcharges resulting from higher interest rate.

Case II:

The examination showed that the creditor required cosigners of all single applicants for car loans without regard to whether or not the individual met the creditor's credit standards without the cosigner. The creditor's written instruction to loan officers did not mention cosigners or the circumstances in which one would be required.

1. To prevent recurrence of the violation, the agency required the lender to:
    - Sign a written agreement that described the violation and the corrective action the lender would take.
    - Circulate a memorandum to all employees advising them of the revised procedure.
    - Amend the written procedures to provide instructions on how single applicants are to be evaluated and when cosigners should be requested, consistent with the acts.
    - Conduct a half-day staff meeting with all loan processors to discuss evaluation of applicants under the acts and how the new procedures apply.
2. To notify the public of the current nondiscriminatory practice, the agency required the creditor to:
    - Direct several advertisements toward single individuals with the message that they can qualify for credit without a cosigner.
3. To correct the conditions caused by the violation, the agency required the creditor to:
    - Remove any illegally required cosigner, or, if a cosigner was needed, offer to allow the borrower to substitute a qualified cosigner of his or her choice.

Case III

The examiner reported that the creditor converted all applications for charge cards to the name of the male applicant and filed and reported the credit history under his name only. Women had to request their credit history under the male co-owner's name.

1. The agency required the creditor to take the following action to prevent the violation from recurring:
    - Sign a written agreement that identified the violation and specified the corrective action the creditor would take.
    - Revise all instructions to employees correcting the procedures for reviewing, recording, and reporting credit.
    - Develop new written procedures for processing credit applications.
2. To correct the conditions caused by the creditor's practice, the agency required the lender to:
    - Identify all affected individuals and notify them of the changes that would be made to their accounts to correct the violation, including an offer to change the names in which the account was held.
    - Notify affected account holders that the information reported incorrectly may have been the cause of a credit denial based on insufficient credit history and advise those individuals that they may wish to reapply.
    - Notify consumer reporting services of the changes, requesting them to correct the credit history.
3. To assure compliance, the agency should schedule a special limited examination after six months to review the creditor's progress under the corrective action agreement.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM

ALLEN J. FISHBEIN

Center for Community Change

12 Sept 90

The Honorable Alan L. Dixon
Chairman
Subcommittee on Consumer and
Regulatory Affairs
SD-534
Washington, DC 20510-6075

Dear Chairman Dixon:

This is in response to your request for additional information to complete the record on the May 16 hearing on mortgage discrimination.

Q.1. The thrift legislation expanded the Home Mortgage Disclosure Act to cover acceptance and rejection data, and the race, sex, and income of the borrower. How will this data be more useful than existing HMDA data? How should it be used? The new HMDA data does not collect information on credit histories, debt-to-income and loan-to-value ratios. How can the new information be useful without this kind of additional data?

A.1. Section 1211 of FIRREA (Fair Lending Oversight and Enforcement) is intended to provide the public with significantly new information about mortgage lending patterns. As the legislative history indicates, the changes are intended "to assist in identifying discriminatory lending practices and enforcing antidiscrimination statutes."

The original law enabled the user to detect neighborhood discrimination (i.e. redlining), especially when the loan data was used in conjunction with census data. However, it could not be used to detect discrimination against individual loan applicants, since it did not require lenders to report any information on borrower characteristics (e.g., race, gender, or income level). Consequently, while it was possible to determine whether or not a loan was made in a minority neighborhood, it was not possible to determine the race or gender of individual loan applicants.

As a result of the changes, the Federal Financial Institutions Examination Council will be providing loan rejection rate information for each lender covered by the act. This information will be presented in a series of tables that will enable the user to determine, by various income categories, whether minorities and women are being rejected at greater rates than whites and men. The data on borrower characteristics will also be cross-tabulated with census characteristics to enable the user to

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determine whether neighborhood factors affect the loan rejection rates for particular categories of borrowers.

In addition, the regulators have indicated that the Loan Application Registers lenders are required to maintain will be available to the public. This will provide analysis for detailed information about every application an institution has received. It will permit a much more detailed analysis of lending practices than was previously available.

Another important change to HMDA, is that the new law requires "anyone in the business of mortgage lending" in metropolitan areas to report. This means that mortgage companies, consumer finance companies, and others that were not previously covered by HMDA must report under the new law. These companies are becoming an increasingly important part of the mortgage market in many cities, but until the law was changed, they companies that were unaffiliated with bank or S&L holding companies were not required to report under HMDA.

Unfortunately, the Federal Reserve Board, which has rule writing authority for HMDA, determined that the $10 million asset threshold requirement that applies to depository lenders also applies to non-depository lenders. As a result, only a handful of new lenders will be covered by the abovementioned change in HMDA. Section 5 of the Fair Lending Enforcement Act of 1990, which you have sponsored, would eliminate this broad loophole and require the Fed to develop a more appropriate threshold requirement for non-depository mortgage lenders.

The new HMDA data is likely to be used by private fair housing organizations, civil rights enforcement agencies, community groups, and the regulators to flag institutions that may be engaged in possible illegal credit practices. The fact that debt-to-income and loan-to-value ratios are not included in the basic data report is not critical to this type of discrimination analysis. Once an institution is flagged, additional analysis by the regulators, or through civil discovery procedures, may be necessary to determine whether the loan was denied on a permissable or impermissable basis.

Q.2. Why do you believe that a separate consumer compliance staff is needed? How will it make a difference? Has it made a difference at the Federal Reserve or the Office of Thrift Supervision?

A.2. Establishing a separate consumer compliance staff is the best way to foster leadership with a strong sense of mission in the consumer, CRA, and fair lending areas. In the days when Truth-in-Lending was the only federal consumer law enforced by the federal banking agencies, it may not have made sense for a set of examiners to specialize in consumer compliance. Today, given the full range of consumer, community reinvestment, and fair lending laws, there is a sufficient level of expertise required to warrant specialization in consumer compliance for a segment of the examiner force.

Full-fledged specialization in consumer compliance -- commonly called a separate career path -- entails separate recruitment, specialized training, and promotion as a consumer examiner. This is the best means to develop the expertise and incentive structure necessary for vigorous consumer enforcement programs. When examiners whose primary function lies in the safety and soundness area are detailed to perform consumer exams, they are not as knowledgeable in consumer compliance as consumer specialists and are less likely to pursue consumer problems with vigor. Also, with specialization there is more incentive for the agencies to develop strong examiner training programs in the consumer compliance areas. Further, a separate career path in consumer compliance enhances the chances that outstanding performance in conducting consumer exams will be rewarded with promotion. Finally, recruitment for positions in consumer examiners is more likely to attract individuals with underlying interests in community reinvestment, civil rights, and consumer protection than recruitment for general examiner positions with its inevitable emphasis on safety and soundness.

The FRB employs full-fledged specialization and a separate career path for consumer examiners. Its examiners are generally recognized as being the most qualified to perform consumer exams. Unfortunately, it is difficult to determine whether the consumer specialists have made a difference in enforcement. Part of the reason is the highly decentralized structure of the Federal Reserve System, which in effect, has a separate consumer compliance program in each of its 12 districts. Consequently, in our opinion the Federal Reserve System does not make the most effective use of the Division of Consumer and Community Affairs, which is based in Washington, DC. This division coordinates and reviews the practices of the individual compliance programs, but it does not directly supervise the compliance examiners. A single, uniform would help to improve enforcement.

We are unable to comment on whether the OTS program is making a difference since it is relatively new.

Q.3. The regulators all report that they had few fair lending complaints. Do you have any recommendations on how to encourage consumers to know more about their rights so that they will file complaints when they detect discrimination?

The U.S Department of Housing and Urban Development, perhaps in conjunction with the regulatory agencies, should undertake a major training program involving private fair housing organizations, civil rights enforcement agencies, and community groups to expand enforcement of the fair lending laws. Increased activity by these organizations will encourage individuals who believe they have been discriminated against to come forward with their complaints.

I hope this reponds to your questions. I would be glad to answer any other questions that your may have.

Respectfully,

Allen J. Fishbein
General Counsel

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM
SHANNA L. SMITH

TO: Kim Shafer
FROM: Shanna L. Smith
RE: Question from Senator Alan J. Dixon - May 16, 1990
DATE: August 20, 1990

Q.1. You testified that the training you provided to lenders in Toledo was very detailed and that often lenders were surprised when you suggested certain policies were discriminatory in effect. Please elaborate.

Policies that have a discriminatory impact include the following:

1. Minimum mortgage loan amounts. Setting a low amount under which the lender refuses to grant a mortgage loan or granting a loan with significantly reduced terms for the length such as five or 10 years instead of longer options. This limitation adversely impacts women and minorities who have lower incomes and can only afford lower priced housing. By restricting the amount and terms of a loan, the lender in effect denies the loan.

2. Tiered interest rates. By charging higher rates for a lower mortgage the lender is unfairly penalizing lower-income persons. This can be measured by looking at the Hispanic and African-American populations within a community and seeing if the tiering of rates or application of minimum loan amounts has a disparate impact on this population.

3. Appraisal guidelines. Using comments on appraisals to reject or change the terms and conditions of loans in minority or lower-income areas. For example, we find terms like "functional utility", "functional obsolescence" "predominant value" used to describe older properties. Appraisers will state that building materials are functionally obsolete and lower the price of the home when in fact what they are describing are plaster walls instead of dry wall and past building quality techniques. However, when homes in predominantly white historic districts are reviewed, these same issues of "obsolescence" are not noted.

Using other innocuous terms like "property lacks marketability" although the property appraised properly and a bid is pending on the subject property.

4. Inappropriately considering the age of housing. Making more restrictive terms for loans for older housing located in the innercity and adjacent integrated and ethnic neighborhoods by reducing the standard 30 year mortgage commitment to 10 or 15 years.

5. PMI. Doing business with only one PMI company and in particular, one that has tough guidelines and/or minimum insurance amounts and failure to submit applications to several PMI companies for review. In addition, failure to work with minority and female applicants or white applicants purchasing in minority/integrated neighborhoods to correct or clarify questions raised by the PMI company.

6. Failure to provide the same degree and quality of counseling to a minority family who applies for a loan and would qualify with some additional information or clarification on credit or employment matters.

7. Failure to report secondary buyers who consistently refuse to purchase properties in minority and lower income areas also contributes to the discriminatory treatment of racially identifiable neighborhoods.

* * *

Then there are the issues of products and services offered by lenders which often have a disparate impact on women and minorities.

1. Savings Accounts: Requiring large amounts of cash ($100.00 or more) to open up a savings account. Many lower income families cannot put $100 initially into an account.

2. Checking accounts: Providing free checking for seniors, but charging lower income persons for service. Several Toledo lenders provide free checking for lower income persons who write few checks per month and add a minimal charge for each check written beyond the limit.

3. Check cashing policies: Charging a fee to cash a government check if one is not a customer of the bank. Toledo lenders no longer charge for cashing any type of government check and you do not have to be a customer. The lenders are suppose to encourage the person to learn about banking services and recruit him/her as a customer.

4. Basic treatment of minority customers. Testing shows that minority customers are required to show identification more often than white customers. White tellers behave as if all minorities are crooks. Toledo is sponsoring a sensitivity training for local lenders in October. This will include white peoples' perceptions and treatment of minorities and how to identify and deal with personal prejudices.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR DIXON FROM ROGER W. JEPSON

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

August 28, 1990

Honorable Alan J. Dixon
Chairman
Subcommittee on Consumer and Regulatory Affairs
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, DC 20510-6075

Dear ~~Senator Dixon:~~ Al —

Thank you for your letter regarding the National Credit Union Administration's (NCUA) procedures for enforcing anti-discrimination laws.

I have attached the Agency's response to the 14 questions you posed in the order presented.

If we can be of further assistance, please do not hesitate to contact me.

With kindest personal regards, I am

Sincerely,

Roger

Roger W. Jepsen
Chairman

Question 1: Discuss briefly your current procedures for enforcing anti-discrimination laws.

The NCUA Board, on a continuing basis, reviews agency goals and evaluates available resources. As a result of this review, NCUA has determined that it can effectively combine a review of credit union compliance with consumer laws with the safety and soundness examination. The NCUA Board has delegated responsibility and enforcement of consumer compliance to the Agency's six Regional Directors.

Compliance with consumer laws is determined by our staff of credit union examiners. Each examiner is provided with specialized training to assure an appropriate level of knowledge of all applicable laws and regulations, including consumer protection laws and regulations. Over the past year, NCUA training efforts in this important area of consumer protection have increased significantly. Each of the Agency's examiners receives detailed information on consumer laws in NCUA's Examiner's Guide. Periodic updates are provided staff in a number of agency communications. In addition, to enhance our ongoing training efforts, we recently provided all examiners with computer based training modules on consumer laws. These modules deal with residential mortgage lending,the Equal Credit Opportunity Act, Truth-In-Lending, and the Fair Housing Act. All examiners are required to achieve satisfactory scores demonstrating proficiency in the enforcement of these consumer laws.

During each examination of every credit union, NCUA examiners are required to complete a Consumer Compliance Checklist (NCUA 2013), designed to aid the examiner in detecting areas of noncompliance.

Copies of the check list prepared during each examination are retained in the Regional Office responsible for supervising the credit union. Periodically, the Office of Examination and Insurance in Washington conducts a review of credit union compliance with consumer laws and regulations. These reviews are accomplished utilizing appropriate sampling techniques. On an annual basis, NCUA reports on credit union compliance to the various regulatory agencies charged by Congress with the administration of the laws and regulations. Copies of our most recent communications with the Federal Reserve Board, the Department of Housing and Urban Development and the Federal Trade Commission are enclosed with this letter. They reflect a high degree of credit union compliance.

Question 2: In how many instances over the past three years has NCUA found substantive violations involving mortgage race discrimination of the Fair Housing Act or Equal Credit Opportunity Act (ECOA) while conducting examinations? Explain how each of these substantive violations was resolved.

Historically, credit unions have been considered pro-consumer, almost by definition. They are member owned, member operated, not for profit cooperatives. The majority are relatively small in size (under $2,000,000 in assets) and do not engage in first lien, residential mortgage lending. In 1989, only 19.5% of all federally insured credit unions granted 1st mortgage, fixed rate loans.

For the purposes of this discussion, we will define a substantive violation of the law as one where a credit union has violated six or more of the provisions of a regulation, rather than an isolated instance of failure to comply with the statute. Anything below that would be an area of concern, but not substantive. This is the same methodology we use to report compliance to the Federal Reserve Board.

In our report to the Federal Reserve Board dated November 3, 1989, we indicated that 89% of all credit unions in our sample were in full compliance with the provisions of the Equal Credit Opportunity Act (ECOA). 11% of the credit unions in the survey had failed to comply with 1 to 5 of the provisions of the Act. No credit unions had met the test of substantive violation. In the 1988 report, we found that 93% of all credit unions in our survey were in total compliance with ECOA. While difficult to document, we attribute this slight reduction in complete compliance to a greater examiner awareness of ECOA rather than an actual decline in credit union compliance.

On February 20, 1990, NCUA reported to the Department of Housing and Urban Development (HUD) that our six regional offices had received no complaints from credit union members pertaining to compliance with the Fair Housing Act.

While we have not encountered substantive violations of ECOA or FHA, it is nevertheless NCUA's policy to require correction of any violation, no matter how small. Once a potential problem is identified, the examiner works closely with the credit union to isolate the problem and obtain agreement on actions. Depending on the extent of the problem, examiner follow-up may be necessary. The extent of the follow-up is determined by the severity of the violation.

Question 3: How many fair lending written complaints involving mortgage race discrimination did NCUA receive over the past three years? How many of these complaints led to a finding of a substantive violation? Explain how each of these substantive violations was resolved.

As indicated above, our regional offices are responsible for the supervision of credit unions in their region. Each region establishes its own method to monitor the number and type of member complaints it receives. Some methods are automated, while others are paper based. It would be difficult, and extremely time consuming, to go back three years to determine the exact number of complaints it has received. We have contacted all of our Regional Directors, and they have indicated that there were no substantive violations of fair lending statutes during the past three years.

To give a better idea of the extent of complaints NCUA receives from credit union members, we asked two regions, that utilized an automated complaint system, to summarize the complaints they have received over the last three years relating to consumer regulations. The results are as follows:

NCUA Region	**Number of Credit Unions**	**Number of Members Served**	**Number of Complaints**
Region I (Albany)	1,839	5.8 Million	41
Region VI (Pacific)	1,235	7.4 Million	38

The types of complaints fall under the following categories:

Regulation B	29
Regulation Z	28
Fair Credit Reporting	14
Regulation E	6
Regulation CC	1
RESPA	1

The number of complaints, in relation to the number credit unions and credit union members, is extremely small. Still, NCUA has the responsibility to investigate any complaint about possible discrimination. We take that responsibility seriously. When a complaint is received, it is reviewed by an analyst in the regional office to determine the validity of the complaint. Regardless of the extent, each complaint is reviewed and resolved. Once resolved, the letter is placed in the credit unions file for any future review.

Question 4: How many fair lending telephone calls did NCUA receive over the past three years? How many involved claims of racial discrimination in home mortgage lending? Can you characterize these inquiries? Are there any patterns among these inquiries? What are complainants told in response?

We do not maintain a log of telephone calls that specifically relates to claims of racial discrimination in home mortgage lending. Our regions have indicated that, to the best of their recollection, there have been no phone calls that specifically relate to this area. This is not surprising, when you consider that if a credit union were to discriminate in lending, it would be discriminating against its own members. Unlike other financial institutions, the individuals making the lending decisions at credit unions are either voted into office by the credit union's members, or are directly responsible to credit union officials (the Board of Directors or Credit Committee) that have been elected by the members.

Question 5: In how many instances over the past three years has NCUA referred cases of possible discrimination to the Department of Justice for prosecution? How many to the Department of Housing and Urban Development (HUD)? What were the results?

NCUA has not referred any discrimination cases to the Department of Justice or the Department of Housing and Urban Development over the past three years.

Question 6: How many hours out of an examination will an examiner spend on fair lending enforcement, according to the size of the credit union? How often are these exams done?

At least once a year, NCUA performs an on-site examination of each federal credit union. Our examination program includes minimum CORE examination procedures. If a problem is identified during the CORE examination procedure, the examiner has the ability to expand that area of the examination to determine the extent of the potential problem.

During each examination, the examiner performs a detailed review of the credit union's lending area. This review includes an analysis of the credit union's lending policies and practices, as well as a review of actual loans. An important portion of the review of lending is the credit union's compliance with fair lending. It is difficult to pinpoint, with any level of accuracy, the precise number of hours an examiner will devote to fair lending enforcement. Each credit union board of directors determines what types of loan products it will offer to its members. The types and complexity of loan products are not always determined by the asset size of a credit union. For this reason, the amount of time the examiner spends in the lending area is determined by the complexity of the loan portfolio, rather than the credit union's asset size. We can assure you that it is NCUA's policy to allow the examiner the time necessary to ensure compliance with all applicable consumer laws and regulations.

Question 7: In your exams of larger credit unions, do you check whether certain minority neighborhoods have higher rejection rates than comparable white neighborhoods?

No, our current examination procedures do not require the examiner to perform an analysis of lending patterns based on neighborhoods since very few credit unions are neighborhood based. Furthermore, examination procedures, such as geocoding, are extremely costly and time consuming. Based on credit unions' track record of an extremely high level of compliance in the area of fair lending and the fact that so few credit unions are neighborhood based, the NCUA Board has determined that a standard examination procedure of this type would not be in the best interests of the either the Agency or the credit union members/borrowers they serve. In the event an examiner believed a neighborhood based or community credit union was rejecting loans based on neighborhoods, our examination procedures would certainly provide the latitude to perform a thorough analysis of this type.

Question 8: Has NCUA found violations of the Fair Housing Act or ECOA based on an "effects test" analysis? Can you provide any specific examples of how you have used this approach to prohibit lenders from maintaining loan policies which have a discriminatory effect on minorities? If your examiners found credit unions which maintained the following loan policies, what would they be trained to do: a minimum loan size? a minimum lot size? a minimum income level? a maximum age of the house? that the neighborhood was stable or improving? How many credit unions have been cited for any of these policies?

We have not found any significant violations of the Fair Housing Act or ECOA based on an "effects test" analysis. During each examination, the examiner performs a complete review of the credit union's written lending policies. During the loan review phase of the examination, the examiner determines if the credit union's actual lending policies follow the written policies. If the examiner determines an existing policy or procedure is being violated, or that, based on an effects test, could be perceived as being discriminatory, the credit union's officials would be made aware of the concern and the examiner would require corrective action.

Certainly the restrictive lending policies posed in question 8 could result in discriminatory lending against minorities. If an examiner ever encountered any such policy or practice, the examiner is required to bring the objectionable policy to the immediate attention of the credit union's officials for remedial action. During the examination, action would be taken to ensure that the potential discriminatory policy is changed. If the officials were to refuse to take the necessary action, the examiner would make a recommendation to the NCUA Regional Director that could result in administrative action against the credit union.

To the best of our knowledge, there have not been any situations where we have found it necessary to cite a credit union for significant effects test situations. On occasion, minor, unintentional problems have been brought to the attention of credit union officials and they have taken the necessary and proper action to correct the problem.

Question 9: Would NCUA detect under-appraisals of properties in minority areas in its normal examination or complaint-response procedures? If a loan were denied because of a low appraisal on the property -- as is often the case in minority neighborhoods -- will the examiner check this in its computerized sampling technique? Will the examiner be able to check whether the appraisal itself was based on illegal discrimination?

Under normal circumstances, an NCUA examiner would not detect an under-appraisal of property in a minority area. Our current examination procedures do not include a computerized sampling technique, nor is the examiner required to cross reference the denial of loans against the appraisal value of collateral. On the other hand, if an examiner noted a pattern of denial based on low appraisals, the latitude is in place to expand the examination procedures to investigate the potential for discriminatory activities.

If NCUA received a complaint that revolved around possible under-appraisals of property in minority neighborhood, the examiner would certainly perform a detailed investigation of the complaint.

Question 10: In light of the recent studies of discrimination in Atlanta, Detroit, Boston, and other cities, what additional steps has NCUA taken to determine whether the disparities in lending between minority and non-minority neighborhoods is attributable, at least in part, to discriminatory lending practices. If no additional steps were taken, why not?

NCUA, and the credit union community, has always been concerned about possible claims of discriminatory lending practices. The very nature of the credit union philosophy is to serve all of it's members. Since each credit union has a defined field of membership, the possibility of an Atlanta, Detroit or Boston situation coming to light in credit unions is somewhat remote. Still, NCUA has take steps to heighten our examiners' level of awareness of discriminatory lending practices. As noted above, we have provided our staff with sophisticated computer based training modules that give specific examples of "effects test" violations. The training program not only provides the examiner with clear cut examples of discrimination, but also points out potential "gray" areas that could lead to discrimination. With this heightened awareness, our examiners are better positioned to determine if disparities in lending are a result of discriminatory lending practices.

Question 11: HUD testified at the October 24, 1989 hearing that the most effective way to detect discrimination is to gather the necessary data and to examine it for patterns of discrimination. What statistical information would prove or strongly suggest discrimination? Do you collect such information? If not, why not? Kindly provide any aggregate HMDA data currently available to illustrate the lending records of credit unions, particularly larger institutions.

The review of a sample of loan applications that have been denied, or referred back to the loan applicant to make modifications to the loan request, would provide the examiner with meaningful information to detect discrimination. During each examination, our examiners review the credit committee and/or loan officer minutes to get a picture of approvals and rejections. A disproportionate number of denied loan applications from minority borrowers would serve as a "red flag" to the examiner.

Our current examination procedures do not require the examiner to maintain a specific record of which specific credit committee/ loan officer minutes have been reviewed. Maintaining such records would result in a significant increase in the time to perform an examination of each federally insured credit union. This requirement has not been made a part of our procedures because the current track record of credit unions, and their philosophy of service to their members, do not indicate a problem in this area.

We do not perform a detailed analysis of currently available HMDA data to illustrate the lending records of credit unions.

Question 12: Will the new statistical information to be gathered pursuant to the recently amended Home Mortgage Disclosure Act (HMDA) be sufficient to strongly suggest discrimination (assuming disparities are present in the data)? Will this data be more useful than existing HMDA data? Will you use it in any way different from existing HMDA data?

We believe that credit unions are not guilty of discriminating against any class of their membership. The new statistical information being gathered pursuant to the recent amendments to HMDA will doubtlessly go a long way to confirm these beliefs. If used correctly, the new data will help all regulators (and the financial institutions themselves) identify discriminatory activities. We believe the current requirements of HMDA are sufficient and will be extremely useful.

We currently have no plans to use the newly available HMDA data differently than the existing data.

We would like to take this opportunity to inform you, and the Subcommittee, of an initiative NCUA has taken to help credit unions comply with the new HMDA reporting requirements. We have developed a PC based program that can be used to accumulate all required HMDA data and produce the required HMDA reports. In July we notified all credit unions of the availability of this program and that they could obtain it free of charge. As of August 10, 1990, over 1,200 credit unions have requested copies of our automated HMDA reporting program. NCUA is the first regulator to provide this type service to the institutions it regulates. We believe this voluntary program begun on our own initiative will result in increased compliance while achieving a reduction in paperwork and a substantial cost savings to credit unions and NCUA.

Question 13: The Center for Community Change has recommended in its testimony that each regulatory agency should adopt regulations similar to the Office of Thrift Supervision's (OTS) nondiscrimination regulation, which prohibits redlining and requires written loan policies to be made publicly available. The OTS believes that requiring all savings associations to make available to potential borrowers their clear, nondiscriminatory loan underwriting standards is a important safeguard to assure uniform application. What do you think of this idea?

For many years NCUA's Rules and Regulations have had an anti-discrimination regulation in place that prohibits discrimination based on ECOA protected classes. The regulation also includes certain provisions of the Fair Housing Law. The regulation does not specifically address redlining since the vast majority of credit unions are not geographically based. The other prohibited areas would certainly cover all potential situations.

Since credit union membership is limited to a specific group of individuals (based on an occupational, residential, or associations common bond), making a credit union's written loan policies available to the general public would be of limited benefit. NCUA's Rules and Regulations do require each credit union to have written lending policies. While not specifically stated in the regulation, we have held that a credit union must make these written policies available to any member that requests them.

We believe NCUA's current position is quite similar to that of the Office of Thrift Supervision. Making written lending policies available to the credit unions members is an important method to ensure uniform application of lending policies and procedures.

Question 14: Do you have any recommendations for eliminating mortgage discrimination or improving fair lending enforcement?

We appreciate the opportunity to comment, but we do not have any recommendations at this time.

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

November 3, 1989

OFFICE OF EXAMINATION AND INSURANCE

Griffith L. Garwood, Director
Division of Consumer and Community Affairs
Board of Governors of the Federal
Reserve System
Washington, DC 20551

Dear Mr. Garwood:

The National Credit Union Administration (NCUA) Board asked that I respond to your request for information on credit union compliance and NCUA enforcement activities relative to the Truth in Lending, Equal Credit Opportunity, Electronic Fund Transfer and Expedited Funds Availability Acts. We are pleased to report that credit union compliance continues to be high during the reporting period (July 1, 1988 to June 30, 1989). We continued to be successful in our efforts to focus on enforcement in all federal credit unions. The following responds to the issues in your request:

a. ADMINISTRATION OF ENFORCEMENT FUNCTION. The NCUA Board, on a continuing basis, reviews agency goals and evaluates available resources. As a result of this review, the NCUA Board has determined that the consumer compliance review can be effectively combined with the safety and soundness examination. Examiners complete our Consumer Compliance Checklist (NCUA 2013) during each examination.

b. EXTENT OF COMPLIANCE. The NCUA Regional Directors have delegated responsibilities and authority regarding monitoring compliance and initiating enforcement activities. Periodically, our Office of Examination and Insurance in Washington completes a review of credit union compliance using sampling procedures. The Consumer Compliance Checklist (NCUA 2013) for all examinations started during a 4-week period were forwarded to the Central Office. The responses to items 2(a) through 2(d) of your letter are based on our most recent sample period. The sample consisted of 277 examinations by the regions. All sizes and membership type of credit unions were included in the sample.

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

Mr. Griffith L. Garwood
November 1, 1989
Page Two

For reporting purposes, we categorize instances of noncompliance on the number of regulatory provisions violated rather than the number of times a credit union violates any one particular provision. For example, a particular credit union in violation of four different provisions of Regulation Z, (although it may have been in violation of one of those provisions in ten instances of granting credit) is reported in the "1-5" category. The results of the sample are:

(1) Percentage of examined credit unions not in full compliance by regulation:

Regulation Z: 92 percent of the credit unions examined during this period were in full compliance with the substantive provisions of Regulation Z. Eight percent or 23 of the 277 credit unions examined during the sample period were not in full compliance with the substantive provisions.

Regulation B: 89 percent of the sample were in full compliance with the substantive provisions of Regulation B; while 30 credit unions, or 11 percent of the sample, were not in full compliance.

Regulation E: Only two of the 277 credit unions examined during the period were found to be in violation of a substantive provision of Regulation E. However, of the 277 credit unions examined, there were only 39 examinations where the examiners indicated that the credit union had electronic funds transfers.

Regulation CC: A sampling of credit union compliance with the regulation is not provided for the reporting period. We update our automated examination program annually and examinations started after October 1, 1989, require a documented review of compliance with this Act. (A copy of each of the examination checklists is enclosed.) The forms will allow us to provide an accurate review and report on compliance. At this time we are unaware of any major violations of the regulation.

(2) Percentage of credit unions having violations, by number of violations:

Regulation	Range					
	1-5		6-25		Total	
	#	%	#	%	#	%
Z	23	8.3%	0	0.0%	23	8.3%
B	30	10.8%	0	0.0%	30	10.8%
E	2	0.7%	0	0.0%	2	0.7%

(3) The provisions of each regulation most frequently noted as not being fully complied with follows: (listed in order of frequency, where more than one violation was noted)

(a) Regulation Z

i. "Credit sale" disclosures are made when the credit union sells and finances credit union owned property (226.18(j)).

ii. Accurate variable rate disclosures made (226.6(a)(2)/226.18(f)

iii. Property insurance excluded from finance charge (226.4(d)(2)).

iv. Finance charge accurately disclosed on closed-end credit (226.18)(d)).

v. Disclosures based on the terms of the legal obligation (226.5(c)/226.17(c))

vi. Disclosed interest rates are those actually used by the credit union (226.7(d)(g)/226.18(e)).

vii. Accurate disclosure of payment schedules and total payments (226.18(g) to (h)).

viii Right of rescission if given when required (226.15/226.23).

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

Mr. Griffith L. Garwood
November 1, 1989
Page Four

(b) Regulation B

i. Adverse action notices contain required information (202.9(a)(2).

ii. Adverse action notices provided (202.9(a)(1) and 202.9(b)(2)).

iii. "Government monitoring purposes" information requested on real estate loans (202.13).

(4) A comparison of the extent of full compliance in the 1988 sample with that of the 1988 sample is shown below:

Regulation	Percent in Full Compliance	
	1989	1988
Z	92%	88%
B	89%	93%
E	99% (95%)	100% (100%) *

*Percentage of full compliance to number in sample where Regulation E applies.

At this time, NCUA has no suggestions or recommendations for amending the Truth in Lending, Equal Credit Opportunity, Electronic Fund Transfer, or Expedited Funds Availability Acts.

Should you require further information regarding credit union compliance, please contact Marty Kushner at (202) 682-9640.

Sincerely,

D Michael Riley

D. MICHAEL RILEY
Director
Office of Examination and Insurance

WPR:wpr
Enclosures

cc: NCUA Board
Executive Director
All Regional Directors

CONSUMER COMPLIANCE CHECKLIST FORM 2013

Charter/Ins. # 67890
Examination Date: 09/30/89
FCU NAME: test fcu
REGION: 4
ASSETS: $0.00

INDICATE (X) IN APPROPRIATE COLUMN YES NO **N/A

REGULATION Z - TRUTH IN LENDING

General

1. Does it appear that the disclosures are based on the terms of the legal obligation? (226.5(c) or 226.17(c))..........
2. Does it appear that the right of recision notice is given when required? (226.15 or 226.23)........................
3. Does it appear that the required disclosures are made when voluntary credit insurance is offered? (226.4(d)(1))......
4. Does it appear that the disclosed interest rates are those actually used by the FCU? (226.7(d)(g) and 226.18(e)).....
* 5. Are disclosures clear, conspicuous, in writing and in a form the member can keep? (226.5(a)(1) or 226.17(a)(1))...
* 6. Are the terms "annual percentage rate" and "finance charge" more conspicuous? (226.5(a)(2) or 226.17(a)(2))...
* 7. Are variable rate disclosures made? (226.6(a)(2) or 226.18(f))..
* 8. Is property insurance properly excluded from the finance charge? (226.4(d)(2))....................................

Open-End Credit

9. Does the FCU offer open-end credit? If not, skip questions 10 through 16...

Initial Disclosure

10. Are the periodic rates and corresponding APR's disclosed? (225.6(a)(2))...
*11. Are the finance charge disclosures made? (226.6(a)(1)-(4))
*12. Are all other initial disclosures made? (226.6(b)-(d))....

Periodic Statement

13. Are the corresponding annual percentage rate(s) and finance charge amount(s) disclosed, and is the corresponding APR disclosed consistently with the initial disclosure? (226.7(f)-(g))....................................
14. Are periodic statements furnished at least every 3 months? (226.5(b)(2))..
15. Does it appear that the billing rights statement is furnished annually or with each periodic statement? (226.9(a))..
*16. Are all other disclosures made? (226.7(a)-(k), 226.8 and 226.9)..

Closed-End Credit

17. Is the finance charge accurately disclosed? (226.18(d))...
18. Is the annual percentage rate accurately disclosed? (226.18(e))..
19. Are the payment schedules and total of payments accurately disclosed? (226.18(g)-(h))..............................

* Indicates form review questions which are to be completed using the Washington and regional office's "Reviewed Forms Listings".
** N/A means Not Applicable or Not Reviewed.
A No answer in any numbered question except #9 indicates a possible violation.

CONSUMER COMPLIANCE CHECKLIST

FORM 2013
Page 2

Charter/Ins. # 67890
Examination Date: 09/30/89
FCU NAME: test fcu
REGION: 4
ASSETS: $0.00

INDICATE (X) IN APPROPRIATE COLUMN — YES NO **N/A

20. Does it appear that "credit sale" disclosures are made when the FCU sells and finances credit union owned property (e.g., repossessed autos)? (226.18(j))...............
*21. Are the disclosures grouped together and segregated from all other information? (226.17(a)(1))....................
*22. Are required terms with explanatory language used? (226.18(b)(d)(e)(h) and (j))..............................
*23. Is the "amount financed" disclosure itemization made or offered? (226.18(c))....................................
*24. Are all other disclosures made? (226.18(a)-(r))..........

Comments:

REGULATION B - EQUAL CREDIT OPPORTUNITY

1. Do loan policies and practices appear to be free from prohibited discrimination/discouragement? (202.4 and 202.5(a))...
2. Does it appear that income is considered as required? (202.6(b)(5))..
3. Does the credit union appear to comply with signature prohibition (such as spouses') requirements? (202.7(d))...
4. Are adverse action notices provided, and do they contain an accurate (as reflected in credit committee minutes) reason(s) for rejection? (202.9(a)(1) and 202.9(b)(2))....
5. Does it appear that "government monitoring purposes" information is requested on real estate loans? (202.13))..
* 6. Are loan application documents free from requests for prohibited information and from requests for information in a prohibited manner? (202.5(c) and (d))................
* 7. Does the adverse action notice contain the required information? (202.9(a)(2))...............................

Comments:

* Indicates form review questions which are to be completed using the Washington and regional office's "Reviewed Forms Listings".

** N/A means Not Applicable or Not Reviewed.

A No answer in any numbered question except #9 indicates a possible violation.